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IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1942.

No. 516

EUNICE E. EASTMAN,
Petitioner,

vs.

GUARANTY TRUST COMPANY OF NEW YORK, ET AL.,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Petitioner, Eunice E. Eastman, respectfully prays that a writ of *certiorari* issue to review the judgment of the United States Circuit Court of Appeals for the Second Circuit, entered in this cause on August 4, 1942, affirming the order of the District Court for the Southern District of New York sustaining respondents' motion for a summary judgment against the petitioner, plaintiff below.

Decisions Below. The decision of the District Court appears in the record at page 129 and is reported in 43 F. Sup. p. 37. The opinion of the Circuit Court of Appeals appears in the record at page 152 and is reported in 130 F. (2) p. 300.

Jurisdiction. The judgment of the Circuit Court of Appeals was entered August 4, 1942 (R. 152). Rehearing was denied on September 4, 1942 (R. 179). The jurisdiction of this Court is invoked under section 240 (a) of the Judicial Code, as Amended by the Act of February 13, 1925.

STATEMENT OF THE MATTER INVOLVED.

Nature of Proceedings. The United States Circuit Court of Appeals sustained respondents' motion for a summary judgment against the petitioner, the plaintiff below, on the ground that the respondent, Guaranty Trust Company of New York, the Trustee of a $30,000,000 note issue, owed no fiduciary duty to the petitioner, a holder of $10,000.00 of said notes, notwithstanding the acceptance of the trust duties by the Trustee, the issuance of the notes, and the sale of the $30,000,000 note issue to the public, including the petitioner, by a syndicate in which a wholly owned Subsidiary of the Trustee participated. The Court of Appeals held that petitioner was in no position to maintain the action for breach of trust against the Trustee because no trust relationship was established as there was no trust *res* in the Trustee's possession (R. 156). The court also held that even if any trust relationship existed, petitioner was not in position to recover as the profit realized by the Trustee was of doubtful value (R. 156). It resolved the doubt in favor of the movants, the respondents. One of the judges concurred in the decision on the latter ground (R. 157).

The Material Facts. Respondent, Guaranty Trust Company of New York, hereinafter called "Trustee", accepted its trust duties (R. 104) under a $30,000,000 note issue dated May 1, 1930 and maturing May 1, 1935, bearing interest at 6% per annum payable semi-annually, and issued by the Van Sweringen Corporation (hereinafter called "Company"). The Company was a wholly owned subsidiary of the Vaness Company (hereinafter called "Vaness"), whose principal officers, O. P. and M. J. Van Sweringen, owned 80% of its stock. The Company also owned the Cleveland Terminals Building Company, which will be referred to as "Subsidiary", (R. 18).

The Company covenanted by the terms of the trust indenture to keep $15,000,000 in "segregated assets" until one-half of the $30,000,000 note issue was paid off (R. 84). The Van Sweringen brothers agreed to supply "assigned securities" in order to maintain the "segregated assets" in liquid condition (R. 105-107). The Company was to hold in trust the "assigned securities" for the benefit of the noteholders (R. 86, 107), and covenanted not to pledge any of its assets under certain conditions (R. 82).

The Trustee affixed its corporate seal in evidence of its acceptance of the trusts thereby created (R. 104). The books and records of the Company were always to be open to the inspection of the Trustee (R. 89) and there were to be delivered to it statements of income and profit and loss annually (R. 90). The Company was required, on request of the Trustee, to furnish detailed information as to all of its acts and it agreed to execute further and additional instruments as may be required by the Trustee. The Trustee was vested with discretion to accelerate the entire $30,000,000 note issue in the event of default

(R. 92).* It had further discretion, subsequent to the acceleration, to waive the default and to rescind and annul the acceleration. The entire $30,000,000 was due to the Trustee on demand (R. 93) and the exclusive right of action was vested in it, including the right to file a claim in bankruptcy (R. 94). The Trustee was empowered to take any action to prevent any impairment of its rights and of the rights of the noteholders. The noteholders were prohibited from maintaining any suits in their own name (R. 96), and in order to require the Trustee to take any action, a demand was necessary by 25% of the outstanding notes conditional upon a tender of indemnity to the Trustee (R. 97). The Trustee was to receive compensation and was given a lien on all of the property for the payment of its fees (R. 101).

The respondents, the Trustee and Morgan, became creditors of the Company's Subsidiary to the extent of $11,000,000 each as participants in a $23,500,000 loan which was made in October, 1930 (R. 19). From such loan there was paid the first semi-annual interest on the $30,000,000 note issue (R. 18-20). Morgan held as collateral for itself and for the Trustee all of the common stock of the Company under the $23,500,000 note of the Cleveland Terminals Building Company (R. 21).

The assets of the Company consisted of its investment in its Subsidiary to the extent of $29,253,066.30, an "open account" due from the Subsidiary in the amount of $27,154,584.03, and in the "segregated assets" amounting to $13,444,674.28 (R. 64). Its debts consisted of outstanding notes of the $30,000,000 note issue in the sum of $26,246,000 plus accrued interest as of October 24, 1931 in the amount of $656,150.00, besides a subordinated claim to its officers in excess of $10,000,000 (R. 64-65). When the

* In such event it was to act as "a trustee of an express trust" (R. 93).

second interest payment became due on November 1, 1931 on the $30,000,000 note issue, no funds were available and there was a threatened collapse of the entire Van Sweringen empire which would have also affected the $23,500,000 note of the Subsidiary in which the Trustee was interested as no funds were available to pay the interest which matured at the same time (R. 19-27).

A default in the $30,000,000 note issue would have enabled the Trustee to accelerate the entire issue, to take action for the application of the "segregated assets" and "assigned securities" in payment of the notes (R. 110-111), to obtain a deficiency for any balance against the Company, and to resort against its assets consisting primarily of the "open account" due from the Subsidiary in excess of $27,000,000. Such claim would have ranked equally with the claim of the Trustee and Morgan against the Subsidiary (R. 42). If the noteholders were aware of such facts they might have demanded such action from the Trustee by the joint action of 25% of the outstanding notes.

To avert the default (R. 28) and to prevent the consequences thereof the Trustee and Morgan (R. 43, 45) secretly worked out a plan whereby the Company would offer to the noteholders to use the cash available out of the "assigned securities", to pay one-half of the notes and to purchase the other half of the notes by the exchange for the common stock. The uncancelled notes so acquired were to be pledged as collateral in lieu of the common stock. By this scheme the noteholders would be deprived of their creditors' position for half of their debt and relegated to the position of common stockholders, and the Trustee and Morgan would have exchanged their role with the noteholders and substituted as creditors by the acquisition of the notes in exchange for the common stock which was pledged with them.

Thereby no action could be taken against the Subsidiary on the open account in excess of $27,000,000 as the only remaining creditors against it were the Trustee and Morgan and the other bankers who participated in the $23,500,000 loan. This agreement which was entered in writing with Morgan (R. 119) was never made public, nor was the fact that the Trustee actively participated in bringing about the accomplishment of the scheme (R. 43-44) ever revealed (R. 56-57).

The plan was carried out. The offer (R. 70) in the form prescribed by the Trustee and Morgan (R. 126) was made. The Trustee and Morgan exchanged the common stock for $13,887,000 uncancelled notes which were obtained as a result of the offer (R. 32). Plaintiff and the other noteholders received 50% in cash out of the "assigned securities" and for the balance of 50% they received the worthless stock (R. 29). The Trustee and Morgan realized out of the "assigned securities" some cash (R. 29-33) and received 12% from the collateral (R. 23) besides a deficiency decree against the Subsidiary in excess of $27,000,000 (See *Re Van Sweringen,* 111 F. (2) 378), and the claim of the noteholder for the deficiency was eliminated.

Opinion of the District Court. The opinion of the District Court in speaking of the "fiduciary relationship" between the Trustee and the plaintiff says (R. 134):

> "Both Morgan & Company and the Guaranty Trust Company, individually, were creditors of the Van Sweringen interests to the extent of $11,000,000 each, under loans made on October 30, 1930. In that situation, as Morgan & Company knew, the Guaranty Trust Company had both an individual fiduciary interest to serve. It thus owed its first duty to its trust, as Morgan & Company also knew."

The District Court, nevertheless, exonerated them from liability because: (1) the "segregated assets" and "assigned securities" were not a trust *res* (R. 136), and (2) Even if it was a trust *res* (R. 141) the proof did not show that the respondents received any part of these securities for their personal benefit.

The Report of the Senate Commission. After the rendition of the opinion by the court but before its final judgment there was received by counsel for the petitioner a printed report from the Senate Commission under Resolution 71, being Part 3 of Report No. 14. This Report was directly opposite to the view of the court pertaining to the motive of the Guaranty Trust Company and Morgan and illustrated the breach of faith and fraud as reported by the Senate Commission. Petitioners' counsel immediately forwarded the Report to the court asking it to reconsider its opinion and, if necessary, he would file a formal motion making the Report a part of the Record. The court refused to consider it and entered its final judgment. This matter was presented to the Circuit Court of Appeals by a formal motion for leave to file copies of the Report which the court denied and failed to consider on appeal (R. 153).

Opinion of Court of Appeals. The opinion of the Circuit Court of Appeals after disposing of the contention that the respondents were guilty of fraud considered the question whether there was a breach of trust. It said (R. 156):

> "Accepting the District Court's interpretation of the complaint as alleging a breach of trust as well as the fraud, we further agree that there was not, nor could there have been, any showing of a trust here. Actually the "Trust Indenture" securing the notes and naming the Guaranty Trust Company trustee

was no such thing. In place of the collateral usually deposited with a trustee, there were assets of the Van Sweringen Corporation which were to be kept segregated — but always in the possession of the company — and there was an agreement by which the Van Sweringen brothers were to deposit additional securities if necessary — but with the company, not the "Trustee." As we have said before, "A trust involves a specific subject matter of *res.*" * * * Here there is nothing upon which a trust can be founded."

The Court also said:

"There is, however, another reason why no action could be proved. For even assuming a fiduciary relationship, the plaintiff has suffered no loss or injury by the exchange. * * * at best the interest would have been defaulted and Guaranty Trust Company would have accelerated the principal. The noteholders would then have received just 50% of the principal plus a worthless stock interest in Cleveland Terminals Building Company plus a doubtful open account of the same company of $27,154,584.03. A glance at the balance sheet of that company shows that even this debt was practically, if not entirely, worthless since the assets of Cleveland consisted of real property that was not enough to satisfy the mortgages and securities pledged to more than their market value as collateral on a note issue. Thus it appears that the plaintiff failed to show, even *prima facie*, any injury resulting from her reliance upon the representations which accompanied the offer she accepted, and for this additional reason the judgment was right."

In the concurring opinion Judge Frank said:

"I concur, but solely on the ground stated in the last paragraph of the foregoing opinion. That is alone enough to sustain the decision. The other issues are less clear and I see no need to consider them."

It should be noted that while the District Court sustained the motion on the ground that the respondents did not benefit from the "offer" (R. 141) the Court of Appeals said that petitioner did not suffer any loss (R. 156, 157).*

The Petition for Rehearing. The petition for rehearing pointed out the existence of the trust relationship even if there were no trust *res* and the loss that the petitioner sustained was substantial and that any doubt must be resolved against the movants (R. 160-167). However, the court denied the rehearing.

QUESTIONS PRESENTED.

1. Whether a trust relationship was established between a noteholder and a Trustee which accepted its trust duties under a $30,000,000 note issue and which certified them as having been issued under its trust powers when they were sold to the public by a syndicate in which the Trustee's Subsidiary participated and which trust agreement vested the exclusive right of action as well as all discretionary duties in the Trustee, or, whether the Court of Appeals was correct in its conclusion that no trust relationship existed because there was no trust *res* in the possession of the Trustee.

2. Whether a summary judgment may be rendered for defendants on the ground that the benefits received by them as fiduciaries were of doubtful value and whether it was the duty of the Court of Appeals to construe Rule 56 so as to resolve the doubt against the movants, the respondents.

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* The opinion is in conflict with the authorities cited in Overfield v. Pennroad Corporation, 42 F. Supp. 586, 587, on the point that the rule of "undivided loyalty" does "not rest" upon the "narrow" ground of "injury" or "damage", but on the "broader foundation" of a wise "public policy".

REASONS FOR THE ALLOWANCE OF THE WRIT.

1. The decision of the Circuit Court of Appeals that no action for breach of trust was maintainable because no trust relationship was established between the petitioner and the Trustee, which accepted its trust duties and certified that it issued the notes pursuant to the terms and provisions contained in the trust instrument vesting the exclusive right of action as well as all discretionary duties in it, so far departs from the accepted general law relating to trusts as to call for the exercise of the Court's power of supervision.

2. The decision affirming the summary judgment against the Petitioner, the plaintiff, on the ground that the benefits received by the respondents from a breach of trust were of doubtful value is in conflict with the decision of the same Circuit in construing Rule 56 that every doubt must be resolved against the movant (*McElwain* v. *Wickmore Spencer Steel Co.*, 126 Fed. (2) 210). The decision is also in conflict with the opinion of the United States Court of Appeals for the District of Columbia (*Miller* v. *Miller,* 122 F. (2d) 209, 212) in the construction of Rule 56.

3. A summary judgment on the ground that the defendants did not benefit from their fraudulent acts or breach of trust may not be affirmed on the ground that the plaintiff did not prove even *prima facie* that she sustained any loss and it was the duty of the court to construe Rule 56 as to resolve every doubt in favor of the petitioner and against the movants. Because of the improper construction of the new federal rules the writ should be issued.

4. The tendency of the courts to look beyond corporate forms to the purpose of the corporate acts and to the persons and human beings who moved and operated in the name of a legal entity for their selfish interest, was entirely overlooked. The principle of fiduciary relationship and obligations resulting from the acts of the parties irrespective of the legal forms, and the cardinal rule that no one may serve two masters, based on the moral obligation to refrain from being placed in a position which would excite a conflict between self-interest and integrity of duty, was brushed aside by a technical construction of the instrument which the Trustee executed and on which faith the public invested $30,000,000. To say that a trust instrument of this nature is "nothing" and thereby exempt the Trustee from liability for breach of trust is not in conformity with sound, equitable principles, and it is contrary to public policy. Therefore, the decision deserves a review by this Court.

5. The question whether an official report of a Congressional Committee may be considered by a court without formally introducing it in evidence in connection with a motion for a summary judgment by defendants when the Report throws light on the subject whether the defendants were motivated by honest intentions and whether they defrauded the plaintiff and violated their trust duties is a question that has not yet been squarely passed on by this court and is of extreme importance in the administration of justice and federal procedure.

PRAYER FOR RELIEF.

Wherefore, the above petitioner prays the allowance of a writ of *certiorari* to the United States Circuit Court of Appeals for the Second Circuit, to the end that its judgment may be reviewed and decided by this Court and reversed with proper directions.

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BRIEF IN SUPPORT OF PETITION.

THE JURISDICTION INVOKED.

The jurisdiction to grant the writ of *certiorari* is invoked under §240 (a) of the Judicial Code as Amended by the Act of February 13, 1925 (43 Stat. 1938, 28 U. S. C. A. §347). The order of the United States Circuit Court of Appeals became final on September 4, 1942 when the petition for rehearing was denied (R. 179).

OPINIONS BELOW.

The District Court rendered its decision on February 26, 1942 (R. 129). Its opinion is reported in 43 Fed. Sup. 37. The Circuit Court of Appeals rendered its decision on August 4, 1942 (R. 152). Its opinion was reported in 130 Fed. (2) 300.

STATEMENT OF THE CASE.

In addition to the statement of the case given in the petition which is adopted here by reference, it should also be stated that the suit was originally brought by three other plaintiffs and the petitioner was subsequently joined as an additional party plaintiff. The entire suit was dismissed for want of jurisdiction and on review it was reversed as to the petitioner who remained as the only plaintiff (117 Fed. (2) 95; *certiorari* denied 313 U. S. 559). After the reversal, respondents filed their answer (R. 11). Plaintiff obtained answers to interrogatories and admissions from the defendants (R. 127), and the respondents took plaintiff's deposition (R. 51). Thereafter,

respondents moved for a summary judgment (R. 14) based on the depositions (R. 51) and their affidavits (R. 15, 36, 47).

Another noteholder (Grace W. York) who did not accept the terms of the offer and who was joined as a plaintiff was also dismissed as a party (117 Fed. (2) 95) and she, therefore, filed a class suit on behalf of the holders of $1,213,000 of notes who did not accept the offer and did not receive anything out of the "segregated assets" or "assigned securities". A copy of the complaint appears in this record at page 168. This suit is still pending but may be defeated as a result of the opinion in the instant case as pointed out in the petition for rehearing (R. 164).

The $30,000,000 note issue and the "offer" were also the subject matter of an investigation by the Senate Committee and is reflected in its Report, Part 3, No. 714 of the 77th Congress. This report was printed subsequent to the rendition of the opinion by the District Court but before the entry of the final judgment. We forwarded a copy of this printed report to the court with a request that it grant a rehearing but the District Court entered the final order without making that report a part of the record. We attempted to make this report a part of the record by a motion in the United States Circuit Court of Appeals but the court denied the motion (R. 153). It is our contention that the District Court, the Court of Appeals, as well as this Court may take judicial notice of the official report of the Senate Commission without making that report a part of the record.*

* See Senate Report No. 714, Part 3, relating to the "1931 crisis" which resulted in the "offer" manipulated by the respondents and the argument under Point V (pp. 44-45, infra).

SUMMARY OF ARGUMENT.

I. The affirmance of the summary judgment on the ground that no action for breach of trust was maintainable by the beneficiary of the trust against the Trustee because no trust relationship was established in the absence of a trust *res* in the possession of the Trustee, is a departure from the general law relating to trusts, and the decision is not in harmony with the well accepted principles relating to duties of trusts and fiduciaries.

II. The affirmance of the summary judgment on the ground that even if there existed a trust relationship plaintiff failed to show even *prima facie* that she sustained any loss as a result of the breach of trust because the assets of the company were of doubtful value, is in direct conflict with another decision of the same Circuit in construing Rule 56 that every doubt must be resolved against the movant.

III. The respondents were guilty of fraud and violated their trust duties and under no theory of law was it proper to sustain their motion for a summary judgment under Rule 56.

IV. The fraudulent offer to exchange was not the offer of the Van Sweringens but the offer of the respondents, Morgan and Guaranty Trust Company, and it is they who committed the fraud and breach of trust.

(a) Where an agent perpetrates a fraud on a third party for the benefit of his undisclosed principal, the third party may sue the principal upon the disclosure.

(b) Even if the offer was that of the Van Sweringens the defendants who ratified the offer and accepted the benefits therefrom are liable.

(c) The fact that neither Morgan nor Guaranty Trust personally defrauded the plaintiff is no defense.

(d) The real purpose of the offer was to avoid the collapse of the Van Sweringen empire wherein Morgan and the Guaranty Trust Company were personally interested and not to save the investment of the noteholders.

(e) It was the duty of the Trustee to protect the interest of the noteholders which it failed to do because of its adverse interest.

V. Federal courts may take judicial notice of official reports of Congressional Committees, and the official report of the Congressional Committee conclusively demonstrates the fraud, the violation of the trusts, and the damage sustained.

ARGUMENT.

I.

The Affirmance of the Summary Judgment on the Ground That No Action for Breach of Trust Was Maintainable By the Beneficiary of the Trust Against the Trustee Because No Trust Relationship Was Established in the Absence of a Trust Res in the Possession of the Trustee Is a Departure from the General Law Relating to Trusts and the Decision Is Not in Harmony With the Well Accepted Principles Relating to Duties of Trusts and Fiduciaries.

The statement of the Court of Appeals (R. 156) that the suit for a breach of trust was not maintainable because no trust was established by the trust indenture and that "Actually the trust indenture securing the notes and naming the Guaranty Trust Company trustee was no such thing" is based on a clear misconception of the law of trusts and the accepted principles governing rights and duties of fiduciaries.

The Trust. In concluding that there was no trust relationship between the Trustee and the noteholders the Court of Appeals overlooked important provisions of the Trust Indenture and applicable principles relating to the law of trusts. The Trust Indenture was executed by the trustee, which affixed its corporate seal "**in evidence** of its acceptance of the **trusts**", thereby "**created**" (R. 104). The notes were certified by it "as Trustee" (R. 79) and the issue was limited to such amounts as may be "delivered to the trustee for authenti-

cation" (R. 80). The issuer was prohibited from mortgaging or pledging its assets and from disposing of any of its cash under certain conditions (R. 82). There was a provision for "segregated assets" and "assigned securities" and the execution of a simultaneous agreement to be delivered "to the Trustee" relating to the performance of the provisions for the segregated assets and assigned securities (R. 85). There was a provision placing property **"in trust"** with the corporation by its principal stockholders and for the distribution "to the Trustee for pro-rata distribution to the note holders" (R. 86). The books and records of the corporation were always "to be open to the inspection of the Trustee" (R. 89) and there were to be delivered to the Trustee statements of income and profit and loss annually (R. 90). The corporation was required "on request of trustee" to furnish "in detail" information as to all of its acts and it agreed to execute "further and additional instruments" as may be "required to carry out the intention of this Indenture" (R. 90). **The Trustee was vested with discretion to accelerate the entire $30,000,000 note issue in the event of default** (R. 92) **and it had further discretion in the event of such acceleration to "waive the default" and to "rescind and annul" the acceleration** (R. 92). The whole amount was payable "to the Trustee" upon demand plus its fees and expenses (R. 93). **The exclusive right of action was vested in the Trustee which was also given the right to file a proof of bankruptcy in its own name** (R. 94.) The Trustee was empowered to take any action "to prevent any impairment" of its rights and of the rights of the noteholders including "power to institute and maintain such suits or proceedings" in matters which "would be prejudicial to the interest of the noteholders" and **"No holder of any notes" was authorized "to institute any suit" at law or in equity** in respect to the powers of the "Inden-

ture'' or **"for the execution of any trusts or power"** or "for any other remedy" (R. 96). A demand for action by 25% of the note holders was conditional upon a tender "to the Trustee" of security "satisfactory to it" (R. 97). The Trustee was entitled to "receive compensation" for all services rendered by it "in the execution of the trusts" thereby "created" (R. 101). It was given a **"lien"** upon all the property for the payment of its fees (R. 101). It was empowered to release the trust instrument upon fulfillment of its conditions (R. 103).

A separate agreement was simultaneously executed (R. 105) in "fulfillment of any of the conditions on which the sale of said issue of notes was underwritten and said Trust Indenture executed" (R. 106), and the Trustee was authorized in the event of default "to institute appropriate proceedings for the enforcement thereof" (R. 110).

The $30,000,000 note issue was **sold** by a syndicate in which the Guaranty Company, a subsidiary wholly owned by the Trustee, participated (R. 16).* One class of the note holders received 50% in cash and lost $13,784,000 of their investment evidenced by the notes which were acquired by the Trustee and Morgan as a result of the exchange (R. 33). **Another class of noteholders have lost their entire investment of $1,213,000** (R. 34). Now, in a suit by a noteholder against the Trustee the court reached a conclusion that no trust relationship was ever established by reason of the foregoing matters and that the Trust Indenture was **"nothing"** as there was no trust **res** and that there was **"no such thing"** as a **trust** and (p. 2201) there is nothing upon which the trust "can be founded".

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* The Senate Report No. 714, Part 3, at page 1020, contains the underwriting agreement to float the loan at a commission of $3,500,000 to the syndicate formed by the Guaranty Company, the wholly owned subsidiary of the Trustee. Morgan was to receive for its share 20,000 in warrants (see page 1038 of the Report).

Query: What was this Trust Indenture upon which $30,000,000 in notes were floated on the market by the Trustee and by its Subsidiary, whereby over $15,000,000 were lost to the investors?

The Fundamental Law. The fundamental law of trusts was completely overlooked by the court. **The right and powers transferred from the note-holders to the Trustee, and the discretionary duties vested in the Trustee are in themselves sufficient to constitute the trust relationship.** Rights and powers are such incidents of a trust *res* as to create a trust relationship. In 65 C. J. p. 235, the author said:

> "While the subject matter of a trust must be lawful definite property, there appears to be no limitation or restriction on its kind or nature, it being the rule that a trust may exist in any property, real or personal, legal or equitable, which is in existence and which, in the eye of the court of equity, is of value. **Thus it is held that a trust may exist in a bond,** money, **promissory notes,** etc." (Boldface ours.)

That a right or power is in itself sufficient to constitute a trust **res** was squarely held by the leading authority on trusts. In Perry on Trusts, vol. 1, section 68, the author describes the properties which may become the subject matter of a trust as follows:

> "At common law no possibility, right, title nor **chose in action** could be granted or assigned to strangers. But in equity the rule is different, and **choses in action,** expectancies, contingent interests, and even possibilities may be assigned, and a valid trust created in them. Equitable reversionary interests stand upon the same ground. Property not owned by the assignor at the time, and not even **in esse,** may be assigned in equity; and **a valid trust** may be created in **a naked power or authority.**" (Emphasis ours.)
>
> See also Bogert on Trusts, section 951.

In Volume 1, Section 2.2, Professor Scott points out that the characteristics of a trust indenture securing corporate bonds is completely different from the characteristics of the ordinary trust and the present Restatement of the Law of Trusts does not deal with trusts securing bond issues and that this will be covered by the future volume of the Restatement of the Law of Trusts. The use of the word "trusts" is frequently employed to indicate duties, relations, which are not strictly and technically trusts. (*Holsapple* v. *Schrantz,* 65 Ind. App. 390, 117 N. E. 547; *Stephenson* v. *Golden,* 279 Mich. 710; *Fox* v. *Greene,* 289 Mich. 179, 183.)

In Jones on Bonds and Bond Securities, Volume 2, section 1030, the author says that the nature and character of trusts assumed by corporations in security bond issues does not merely depend upon the express terms of a trust indenture "but upon the implications, as well, which arise from the relations of the parties and the condition and nature of the trust property", and in section 1053, at page 492, the author says:

> "In general, the duties of a trustee under an indenture securing the payment of corporate bonds are comparable, though not at all points parallel, to those assumed by one undertaking to perform any other trust".

The author further says at page 493:

> "There are, however, duties with which all trustees in corporate mortgages are burdened. They are not mere stakeholders, with the negligent responsibilities that attach to such an office."

Article IV of the trust indenture gave discretionary power to the Trustee to accelerate the note issue in the event of default or in the event of insolvency. Section 24 of the trust indenture (R. 94) **vested the exclusive right**

of action in the Trustee and the Trustee was even vested with the right to file a proof of debt in its own name and the company agreed to pay the Trustee's fees (R. 95). To say that an instrument of this kind lacked a **res** as to strip the instrument of the characteristics of a trust, **is to do violence to the very instrument which was drawn by Trustee.** This question was decided adversely to this contention in *Farmers Loan & Trust Co.* v. *Lake Street R. R. Co.,* 173 Ill. 439 (reversed on another point in 177 U. S. 51). On page 452 the Court pointed out that the trust instrument which vests discretionary duties in a trustee is an **active trust.**

The opinion cites (R. 156) *Bradford* v. *Chase National Bank,* 24 F. Sup. 28, on the point that there must be a trust **res** to create a valid trust. There, it said: "There must be an asset—whether it be land, a chattel or **a chose in action**—in order to have a trust of any kind, express, implied in fact, or impressed by law". **The $30,000,000 in notes constituted choses in action** and was a trust **res** establishing the trust or **fiduciary relationship between the noteholders and the Trustee.** There were certainly some rights conferred upon the Trustee and some limitations were placed upon the corporation by the trust instrument. Such **right** constituted a trust **res** (Bogert on Trusts, section 17, page 74). **A note or a bond** is a "thing" or a "**res**".

Judge Bright called the document (R. 136) "**a peculiar instrument**".* Section 16 of the trust instrument (R. 85) recites that the corporation "has obtained the execution and delivery to the trustee of an agreement by O. P. Van Sweringen and M. J. Van Sweringen with the Trustee for

* See Report No. 714, Part 3, of the Senate at page 889 under the heading "Some Things the Public Did Not Know", and under its discussion of "The Indenture".

the benefit of the holders of the note by which the Van Sweringens will jointly and severally undertake and agree that whenever from time to time the aggregate value of the unencumbered shares of the common stock of Alleghany Corporation * * * shall be less than 50 per cent" of the outstanding notes they would "repair such deficiency by assigning and delivering or causing to be assigned and delivered to the company readily marketable securities to an amount sufficient when taken at their current market value to equal the amount of such deficiency". This **contract constituted** a trust **res** (Bogert on Trusts, section 17, page 74). This agreement related to the "assigned securities" **which was not the property of the corporation** but was the personal property of the Van Sweringen brothers. **Here was a specific res which was delivered to the Trustee under the terms of the trust instrument.** The provision in the trust indenture which stated that limitations shall not be treated as a pledge or mortgage related to the "segregated assets" but **not to the "assigned securities".** It did not exclude the existence of a trust.

The Trustee **entered upon its active duties** and actively participated for the alleged protection of the noteholders (R. 48). A trustee who enters upon its duties at such a stage cannot claim that its duties were passive (*Straus* v. *Chicago Title & Trust Co.,* 273 Ill. App. 63). There it was said (p. 71):

> "It would be absurd to regard the trustee's duties as terminated at the very time when his protection was most needed".

The court therefore clearly erred in holding that there was no fiduciary relationship between the Trustee and the noteholders.

II.

The Affirmance of the Summary Judgment on the Ground That Even If There Existed a Trust Relationship Plaintiff Failed to Show Even Prima Facie That She Sustained any Loss As a Result of the Breach of Trust Because the Assets of the Company Were of Doubtful Value Is in Direct Conflict with Another Decision of the Same Circuit in Construing Rule 56 That Every Doubt Must Be Resolved Against the Movant.

The second reason for the affirmance of the summary judgment is based on the ground that even if there existed a fiduciary relationship between the parties and there was a breach of trust, petitioner did not show "even *prima facie*" that "any injury" resulted to her.

The District Court sustained the summary judgment on the ground that the Trustee and Morgan did not receive any benefits as a result of the offer (R. 141). Our brief in the Court of Appeals pointed out the benefits which the Trustee and Morgan received. The Court of Appeals was evidently satisfied that the Trustee did receive some benefits and, therefore, affirmed the summary judgment on the ground that there was no "*prima facie*" case of "injury", overlooking that there was no opportunity to offer proof as the matter was heard on the motion for the summary judgment.

The reasoning for the conclusion that there was no "injury" to the petitioner appears from the statement of the Court (R. 156, 157) that if petitioner had not accepted the offer and resorted to the "segregated assets" and "assigned securities" and realized therefrom 50% in cash, she would not have realized anything on the

deficiency for over half of the debt out of the assets of the company which consisted primarily of "a doubtful open account of the subsidiary company of $27,154,-584.03". Of course, the "open account" was **never doubtful.** What the court meant to say is that the **value** of the open account was doubtful.

In the concurring Opinion by Judge Frank he stated that he based his concurring opinion on the last paragraph and not on the other issues which "are less clear".

The matter was not decided on a **trial but on defendants' motion for a summary judgment.** The motion had to fall or stand on **its own strength** and not on any weakness in plaintiff's position.

A movant is not entitled to a summary judgment **unless the conceded facts show beyond any doubt** that the plaintiff is not entitled to *any* relief (*Clair* v. *Sears, Roebuck & Co.,* 34 F. Supp. 559). The opinion of the same circuit (*McElwain* v. *Wickwire Spencer Steel Co.,* 126 F. (2) 210) is to the same effect and is **squarely in conflict with the opinions in the instant case.** (See also *Miller* v. *Miller,* 122 F. (2d) 209, 212, construing Rule 56.)

There was nothing in plaintiff's pleading justifying a conclusion that she did not sustain damages. There was nothing in defendants' pleading relating to the claim that plaintiff did not sustain any damages. The court determined such facts from a "glance" at the balance sheet and concluded that the asset in excess of $27,000,000 consisting of the "open account" against the Cleveland Building Terminals Company was "a doubtful open account", or, in other words, **of doubtful value,** so that if the exchange was not made, the noteholders would have received in addition to the 50% in cash, **assets of a doubtful value.** Even if this be so, the defendants would

not be entitled to a summary judgment **as every doubt must be resolved in favor of the plaintiff.** However, there is no foundation for the Court's determination.

The Complaint alleged (R. 8) that it was known to the defendants that "the open account in excess of $27,000,000 was not fully collectible". The Answer of the defendants **denied** this allegation (R. 13). **Their denial can only be construed to the effect that the defendants did not know that the open account in excess of $27,000,000 was not collectible.** The Bankers who filed their sworn answer had the same balance sheet before them so that they could have had a "glance" at such balance sheet, yet they stated in their pleadings that they did not know that the $27,000,000 was not fully collectible. The Trustee and Morgan were interested in the assets of the subsidiary and the value thereof was not "doubtful" to them. They sought to prosecute their claim against the subsidiary as it appears from an appeal taken from the allowance of the claim filed by Morgan on behalf of itself and the Trustee (*Re Van Sweringen,* 111 F. (2) 378). It also appears from another appeal that Midamerica, which purchased the $13,784,000 in notes from Morgan, endeavored to establish its claim against the Cleveland Terminals Building Company and was interested to appeal from the decision of the trial court (*Re Van Sweringen,* 119 F. (2d) 231), and was also interested in applying for writ of *certiorari* to this Court, where its application was denied (314 U. S., page 671). **The claim was evidently not of doubtful value.** Incidentally, the Cleveland Terminals Building Company was reorganized; none of the mortgages were foreclosed; and the equity of the company for the benefit of its general creditors is of substantial value. Therefore, the open account in excess of $27,000,000 which would have ranked "equally" with the

claim of the Trustee and Morgan against the reorganized Cleveland Terminals Building Company (R. 42) was and is of **substantial value.** At any rate, the court was in no position to determine such value on the summary judgment for the defendants.

III.

The Respondents Were Guilty of Fraud and Violated Their Trust Duties and Under No Theory of Law Was It Proper To Sustain Their Motion for a Summary Judgment.

The Van Sweringen brothers, who controlled the entire empire, were fiduciaries of the noteholders, the creditors of the company, in view of the insolvency of the company. (*Younglove* v. *Lima Co.,* 49 O. S. 663; *Thomas* v. *Matthews,* 94 O. S. 32, 47). The "offer" operated for the personal benefit of these fiduciaries as well as for the benefit of the Trustee and Morgan. Even if there was no trust relationship between the Trustee and Morgan and the noteholders, they were in the capacity of fiduciaries under the rule that if third persons enter into agreements with fiduciaries resulting in benefits to the fiduciaries, **such third persons stand in the capacity of fiduciaries** and must account for the profits realized by the fiduciary. This doctrine was recognized by the District Court (R. 142) which cited *Irving Trust* v. *Deutsch,* 73 F. (2) 121. See also *Re Van Sweringen Corporation,* 119 F. (2) 231, 234. However, the Trustee and Morgan **directly benefited** from the transaction, which resulted in **loss** to the plaintiff.

The total amount of the "segregated assets" and "assigned securities", according to the "offer" (R. 71) aggregated $13,440,681.86. Based on the outstanding

notes of $26,234,000 and accrued interest of $787,290.00 there was required in "segregated assets" a total of $13,894,290 so that there was a deficiency in such assets in the amount of $453,618.20 which the Van Sweringens were obligated to make good.

If they did not supply this deficiency, the Trustee had the right to accelerate the entire note issue. In such event all of its "segregated assets" and "assigned securities" would have been applied in part payment of the $26,234,000 notes. The note holders would have then received 50% in cash out of the "segregated assets" plus a deficiency for the balance. **They could have resorted then to the remainder of the assets of the Van Sweringen Corporation** consisting of the entire capital stock of the subsidiary which they **scheduled at cost in excess of** $29,000,000 (R. 64) and they could have resorted to the enforcement of the **"open account" against the Subsidiary in excess of** $27,000,000 (R. 64). Such a procedure would not have been in the interest of the **fiduciaries,** the Van Sweringens, the "Guaranty Trust" and its partner in the loans, Morgan. This would have thrust the Subsidiary into bankruptcy in 1931, and they would not have been in position to manage and operate up to 1936 when they finally landed in bankruptcy.* Morgan and Guaranty Trust Company, **who were behind the scene, made the "offer" possible.** The Van Sweringen Corporation and its officers were their **agents,** and **they,** the defendants, the **undisclosed principals,** are liable to the plaintiff for the damage caused to her in exchanging her notes for the worthless stock which **they supplied.**

* It should be noted that the Van Sweringens managed to receive $100,000 annually from 1931 to 1936 and that they had a direct personal gain to such extent (Re Van Sweringen, 119 F. (2) 231).

Morgan and Guaranty Trust Company Exchanged the Worthless Stock for the Notes.

All common stock of the Van Sweringen Corporation was pledged as collateral under the note which was jointly owned by Morgan and Guaranty Trust Company. They participated in bringing about the "offer" which enabled them to substitute the pledged worthless common stock for $13,784,000 notes of the $30,000,000 note issue (R. 33).* It is **they who received plaintiff's $5,000.00 notes and gave in exchange therefor the 200 shares, which they knew to be worthless.** In order to accomplish this exchange **they** caused the balance sheet to be made up which showed the value of the common stock to be $32,773,638.28 (R. 65).** **They knew that the stock was valueless.** This is confessed by the affidavit which states that a "study" of the balance sheet revealed such facts (R. 40). **They did not disclose the result of their study and analysis to the plaintiff in the "offer" that they caused to be submitted to her. They did not disclose to her the fact that the corporation had no funds to meet the interest payments and if bankruptcy followed the stock would be worthless, which facts were known to them as is shown by the affidavit** (R. 43). On the contrary, the form of the "offer" which **they** prepared stated that interest would be paid in the **"usual"** way at the office of the Guaranty Trust Company (R. 72, 73). **This led the noteholder to believe that the corporation was in good standing and that the stock had some value.**

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* The form of the offer was prepared as part of the agreement with Morgan as Exhibit "A" (R. 123, 126). This offer stated (R. 72) that this balance sheet "will be furnished on request".

** The defendants were clearly liable under the rule that where two persons who occupy a fiduciary relation to a third person enter into a transaction with "each other" whereby one of their agents acquires the property of the third person "to his own advantage", such transaction is "contrary to public policy" and is "prima facie fraudulent" (Rothman v. Wilson, 9 Cir., 121 F. (2) 1000).

In order to arrive at the valuation of the stock in excess of $32,000,000 it was necessary to show in the balance sheet the investment in the subsidiary at **cost** in the amount of $29,253,066.30 and to include the "open account" against the subsidiary in the face amount of $27,154,584.03 (R. 64). This was done in **violation of the terms of the trust indenture** which provided that values were to be carried at "**existing market value**", or at "**fair value**" when no market was available (R. 83). It is true that the balance sheet contained in **small type** (R. 66) in footnote 2 the market value of the securities. **These marginal notes are hardly understandable to the average investor.** No fair value of the real estate was given. **They featured the value of the capital stock in large capital letters** (R. 65). While the expert banker might, as a result of a "**study**" and "analysis" of the balance sheet, **detect** that the corporation was insolvent, **as they did** (R. 40), and while the Judges of the Court of Appeals were able to ascertain such facts from a "glance" at the balance sheet, the average investor could not be expected to do that. Plaintiff, according to her testimony, was not a business woman and **did not understand the balance sheet** (R. 55) **and was of the opinion that she was getting value when she received the stock** (R. 57). She said, "**I assumed that the stock was worth half of my notes because they gave me half money and half stock. It was half and half**" (R. 57). The depositions which defendants offered in support of the summary judgment were **conclusive on them.** Morgan and Guaranty Trust Company had actual knowledge that the stock was worthless.* **They entered into an agreement to publish the offer** for the benefit of the Van Sweringens and for their own

* The fact that the "victims" might have "discovered the cheat" is immaterial when the parties did not have equal means of knowledge (Falter v. U. S., 23 F. (2) 420, C. C. A. 2).

benefit, and **concealed the true facts.** They cannot escape liability for such conduct.

In discussing another phase of the situation involving the subject of the sale of the same $13,784,000 notes by Morgan on September 30, 1935, to Midamerica, a corporation organized by the Van Sweringens, the Sixth Circuit said *In re Van Sweringen Corporation,* 119 Fed. (2) 231, at page 234:

> "It seems soundly settled that one who knowingly joins a fiduciary in purchasing for profit the property of the trust estate in unlawful circumstances, became jointly and severally liable with him for the resultant profit."

Here, not only did Morgan join with the Van Sweringens for their own benefit, but also for the benefit of the Guaranty Trust Company **to obtain the exchange of the pledged worthless stock for the 13,784,000 notes** to be held as security under the joint note of Morgan and Guaranty Trust Company. Their liability is not only based on the benefits resulting to Van Sweringens as fiduciaries, but on the personal benefit which **they derived out of the fraudulent transaction.** Van Sweringens and the Corporation were their instrumentalities or agencies to make the offer under the agreement. They, the defendants, concealed these material facts from the plaintiff, and **the concealment of these facts constituted fraud in equity.**

The opinion of the District Court says (R. 142):

> "We can, however, **assume there was a trust relation,** and apply the now oft-quoted statement of Chief Judge Cardozo that, **'A trustee is held to something stricter than the morals of a market place,'** and that 'Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by "disintegrating erosion" of particular exceptions.' (*Meinhard* v. *Salmon,* 249

N. Y. 458, 464). **One who joins with a fiduciary in a breach of trust is also responsible.** *Jackson* v. *Smith,* 254 U. S. 587-589. *Irving Trust Co.* v. *Deutsch,* 73 F. 2, 121, cert. denied, 294 U. S. 708."

After stating this rule, it said:

> "There still remains the question whether there was such action on the part of the defendants which made them liable to the plaintiff. They did nothing the trust indenture forbid. **They did substitute in their collateral the balance of the notes for the stock of the Company.** What the stock was then worth was problematical. Both sides now admit that it was worthless, but who could then tell?"

The Court of Appeals while it affirmed the decision answered the question by saying that it could tell then that the stock was valueless (R. 156).

The affidavit of the defendants in support of the summary judgment also stated that the analysis of the balance sheet of September 30, 1931, showed that the stock was worthless (R. 40). Whether plaintiff understood the balance sheet, as she said she did not (R. 55), may be open to question, but certainly **the persons who prepared the balance sheet, who analyzed it and who were the bankers who floated these loans—they knew the real facts and that the stock was worthless** (R. 40). **They had no right to unload on the noteholders the worthless stock which they held, in exchange for the valuable notes which the noteholders owned.**

The opinion of the District Court stated (R. 142) that the defendants were seeking "to avoid the demolition of the Van Sweringen empire for the benefit of all concerned" and they insured payment to the plaintiff "more than the then market value of the stock" (notes.)* The

* The motive of the Trustee is no defense for the breach of a trust (White v. Sherman, 168 Ill. 589).

District Court asked: "Was there a breach of that high degree of good faith which the law requires of a fiduciary?" It answered: the Trustee could have said "No" and had it taken that position the plaintiff would not have benefited from such a position. It says that the Company might have been able to finance the payment of interest, thereby preventing the default, and used the "segregated assets" to purchase the notes at market prices which declined until it had 50% of the notes, when the Company could have released the "segregated assets". The Court of Appeals was also influenced by such an argument (R. 156). **A Court may not assume a condition different from what the facts were,** particularly on a motion for a **summary judgment when every assumption must be in favor of the person against whom the summary judgment is entered.** The facts as they appear were that the corporation was unable to raise the $900,000 in interest (R. 27). The "offer" which they made on October 30, 1931, was only **one day** before the interest was due—November 1, 1931. How was it possible for the company to raise in one day the required interest and to accomplish such a miracle? **There is also no proof that the noteholders would have sold $15,000,000 notes at a declined market. Failure to obtain $15,000,000 notes would have prevented the release of the "segregated assets". The court had no right to assume a state of facts which might not have accrued in order to defeat the cause.**

The District Court said (R. 143) that bankruptcy might have followed and plaintiff would have had a claim "as a general creditor". It overlooked that **there was no possible chance for a bankruptcy to be instituted** against the Van Sweringen Corporation. The noteholders were the **only** creditors (R. 65). True, the Van Sweringens were also creditors to the extent of $10,178,506.54, but their

notes were **subordinated** to the note issue and did not mature until "May, 1935". There was also a **contingent** claim of $8,000,000 (R. 65) but this **contingent creditor could not have instituted a bankruptcy proceeding** (*Re Howell,* 215 Fed. 1, C. C. A. 2; *Re The Literary Digest,* 105 F. (2) 957; *Manhattan* v. *Irving Trust Co.,* 291 U. S. 320).

The only existing creditors who could have maintained insolvency proceedings were the noteholders but **their notes were not due and the right to accelerate as well as the right to commence any action was exclusively vested in the Trustee. The Trustee was the only party who could have maintained an action to obtain judgment on the $30,000,000** note issue, to appropriate the "segregated assets" and "assigned securities" to satisfy one-half of the debt, to obtain a deficiency judgment for the balance, and enforce it against the assets of the Van Sweringen Corporation which consisted of its stock in the subsidiary at an investment of $29,000,000 and to the "open account" against the subsidiary in excess of $27,000,000. This was not in the interest of the Trustee and Morgan, who were creditors of the subsidiary to the extent of $11,000,000 each because **the noteholders would "rank equally" with them as creditors of the subsidiary** (R. 42). **This is why the Trustee and Morgan caused the offer to be submitted in the name of the Van Sweringens,** but in reality for their own benefit. **This came from their own mouth.** Mr. Shriver stated in his affidavit (R. 42):

> "So far as concerned the New York Banking Group (Guaranty Trust and Morgan) * * * if there were a deficiency in the collateral (under the $23,500,000 note) after a forced sale * * * this claim (of the Trustee and Morgan) **would rank equally with Van Sweringen Corporation's claim for approximately $27,000,000 against Cleveland Terminals Building Corporation.**"

Here was **the real motive** behind the "offer" to prevent this $27,000,000 claim, by excluding the noteholders as **creditors,** and relegating them to the position of **stockholders.**

It was asserted below that the moving consideration for the offer was "to stop the private purchase of notes by the Van Sweringen Corporation with the 'segregated assets'" which was permissible under the terms of the indenture and the opinion seems to have adopted such view (R. 156). **If they really wanted to stop the purchase of these notes at 30 cents on the dollar they could have notified the noteholders that there was available for them 50 cents on the dollar from the "segregated assets" besides the remainder of their pro rata share in the $69,000,000 worth of assets of the corporation for the remainder of the 50 per cent.** A noteholder who would have received such information would not have sold his notes for 30 cents on the dollar. It was necessary to acquire $15,000,000 of the notes in order to release the "segregated assets". **Certainly $15,000,000 in notes could not have been acquired at 30 cents on the dollar if the Trustee had given the information to the noteholders that more than 50 cents per dollar was available for them.***

Why was the Guaranty Trust Company so alarmed (R. 24) if it be true that there was no trust relationship, that there was no responsibility upon it and that its trust was mere routine? The answer is plain. The Trustee knew from its "study" that the Van Sweringen Corporation was then insolvent. The Trust agreement provided (R. 91) that in the event of insolvency or in the event the company shall admit its inability to pay its debts when

*In fact the bankers threatened the Van Sweringens with such action and obtained their commitment that they would not purchase the notes as shown in Senate Report No. 714, Part 3, pp. 974-975.

they became due that the Trustee may declare the entire amount due and take the proper action, and it provided that in such event (R. 93) that the Trustee was then to act **"as a trustee of an express trust"**. The Trustee was also not unmindful of the fact that its position was then **adverse and delicate.** That is why it was **alarmed** and **it was its duty to at least disclose the information to the noteholders.**

IV.

The Fraudulent Offer to Exchange Was Not the Offer of the Van Sweringens But the Offer of the Respondents, Morgan and Guaranty Trust Company, and It Is They Who Committed the Fraud and Breach of Trust.

The "offer" which was submitted to the plaintiff as well as to the other investors was ostensibly an offer of the Van Sweringen Corporation. **In reality it was the offer of Morgan and the Guaranty Trust Company.** Morgan entered into the **secret** agreement to transmit the offer to the public (R. 119). The form of the offer was incorporated in the agreement (R. 70, 126). Morgan and the Guaranty Trust Company **undertook to make the common stock available for the exchange under the offer.** It is **they** who had the common stock as security for the collateral. **It is they who wanted to exchange the pledged worthless common stock for the valuable notes** and who **obtained such notes.** It was they who concealed the true facts and who **obtained the benefits resulting from the offer.**

The affidavit of Whitney states that Morgan and the Guaranty Trust Company each loaned $11,000,000 as part of the $39,500,000 loan which was made to save the Van Sweringen "Empire". The common stock was placed with Morgan as security for such loans. The affidavit further states (R. 28) that a conference was held with

the Bankers in which Morgan and the Guaranty Trust Company participated and that **as a result of these conferences "these general terms having been worked out among the parties named,"** the Van Sweringen Corporation prepared the terms of an offer of purchase for noteholders. It also states **that this offer was examined by Whitney and "by officers of Guaranty Company of New York and of Guaranty Trust Company of New York"** (R. 20). This "offer" was made a part of the secret agreement (R. 126). **The Guaranty Trust actually participated in the preparation of the offer** (R. 48, 49). It is, therefore, obvious that this "offer", which was made ostensibly in the name of the Van Sweringen Corporation, **was in reality the offer of Guaranty Trust and Morgan,** who were the **undisclosed** principals and stood behind the scene. The Van Sweringen Corporation was their tool and instrumentality, and the Trustee and "Morgan", as undisclosed principals who received the benefits, are clearly liable (*Adams* v. *Collier,* U. S., 8 Cir., 73 F. (2) 975, 977).

(a) Where an Agent Perpetrates a Fraud on a Third Party for the Benefit of His Undisclosed Principal, the Third Party May Sue the Principal Upon the Disclosure.

A reading of the secret agreement of "Morgan" (R. 119) and a study of the facts as they are revealed from the affidavits, as discussed above, demonstrates that the Van Sweringen Corporation was the instrumentality and **agent** of Guaranty Trust and Morgan to obtain the exchange of the worthless pledged stock for the valuable note to be substituted as collateral for their personal gain. Van Sweringen Corporation, **their instrumentality,** did not disclose in the offer which the Trustee and Morgan prepared that it was acting for Morgan and Guaranty Trust. On the contrary, it was stated in the offer

(R. 71-2) that "the stock to be delivered to the noteholders * * * will be furnished by the Van Sweringen interests." This statement either referred to Morgan and the Guaranty Trust as synonymous with "Van Sweringen interests" or was a deliberate misrepresentation as the stock was to be delivered under the secret agreement by Morgan (R. 122). **It was Morgan and the Guaranty Trust Company which caused the misleading offer to be mailed to all noteholders including the plaintiff.*** It is **they** who prepared the "offer" which stated (R. 72) that "the notes acquired after the retirement of $15,000,000 will be acquired, not by the corporation, but by the Van Sweringen interests." Why did they not state that this will be acquired by Morgan and the Trustee, whose duty it was to protect the noteholders? Why did they use the words "Van Sweringen interests" instead of "Morgan and Guaranty Trust"? **Because of their adverse interests and fiduciary relation it was their duty to speak,** particularly when they had actual knowledge that the stock which they were going to exchange for the notes was worthless,** and that it was done for the purpose of avoiding the bankruptcy of the subsidiary which would greatly affect the interest of Morgan and the Trustee as its creditor. The fraud of the Van Sweringen Corporation was **their fraud,** as the Van Sweringen Corporation **was their agent** and they, Morgan and the Trustee, were the undisclosed principals. Upon the disclosure of the undisclosed principals the plaintiff, as well as the other noteholders, were entitled to recover from the undisclosed principals.

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* One who knowingly and intentionally clothes another with power to commit a fraud, and knowing that such fraud is being committed, remains silent, is liable (Raymond v. Sec. Realty Co., 91 F. (2) 163, 172).

** Where duty to "speak" exists, suppression of truth is actionable (Kershaw v. Julien, 32 F. (2) 528).

In *McIntire* v. *Pryor,* 173 U. S. 38, 52, the rule was announced that where frauds are committed by an agent in procuring title to property for the benefit of its principal the principal is chargeable therewith in the same manner as if he had committed them personally. The authorities are collected in 2 Amer. Jur. Sections 393, 394. See also Restatement of the Law of Agency, Section 188.

It should also be noted that the Company was actually insolvent at the date of the offer. Being insolvent, it was then Trustee for its creditors. In making the offer to its creditors it was the duty of the Company to disclose all material facts. The defendants who caused the offer to be made by the Company and who were instrumental in having it conceal the facts from the plaintiff and the other creditors and who derived a benefit therefrom are, therefore, clearly liable. (*Conner* v. *Craig,* 4 Cir., 216 Fed. 729.)

(b) Even If the Offer Was That of the Van Sweringens the Defendants Who Ratified the Offer and Accepted the Benefits Therefrom Are Liable.

The affidavit of Shriver stated (R. 39) that the banking group, which included Morgan and "Guaranty Trust," was in position "to throw the borrowers into bankruptcy" by calling the loans if the interest was not paid by November 1, 1931, and that the "borrowers" were in no position to pay such interest. The "study" of the balance sheet of the "parent" and its "subsidiary" disclosed to them that both were insolvent (R. 40). In the event of bankruptcy **the noteholders would not have received half of their debt** according to this affidavit (R. 43). The conclusion that **they** reached that the "assigned securities" and "segregated assets" would not be sufficient to pay half of the $30,000,000 note issue **was clear**

knowledge on their part that the common stock of the Van Sweringen Corporation **was worthless.** With knowledge of such facts they permitted the offer to be made, and **accepted the benefits therefrom in exchanging their worthless collateral for the valuable notes.** Under such circumstances they are clearly liable (*Paige* v. *Keeves,* 362 Ill. 64, 74; *Goldsmith* v. *Koopman,* 152 Fed. 173; *Great Lakes Towing Co.* v. *Mills Trans. Co.,* 6 Cir., 155 Fed. 11, 21).

(c) The Fact That Neither Morgan Nor Guaranty Trust Personally Defrauded the Plaintiff Is No Defense.

There are some references in the affidavits that the plaintiff has admitted by her depositions that she received no communications from either Morgan or from the Trustee and that she admitted that the defendants did not personally defraud her. This is no defense to the action, as the act of their agent is the act of the principal, and when plaintiff discovered the undisclosed principals when she was invited by the original plaintiff to join as a party (R. 74) she was entitled to sue and to recover.

In *Zimmern* v. *Blount,* 238 Fed. 740, the Court said (p. 743):

> "Nor is it necessary that a fraud be personal to the defendant. It is sufficient if committed by his agent and he profit by it."

See also *United States* v. *Carbon County Land Company,* 46 Fed. (2) 980, 987.

In *Brach* v. *Moen,* 35 F. (2) 475 (Certiorari denied 280 U. S. 613), the rule was thus stated:

> "One who **accepts the fruits of fraud** with knowledge of the misrepresentations or **concealment** by which they were obtained will be held liable thereafter, **even though he did not personally participate in the fraud.**"

(d) The Real Purpose of the Offer Was to Avoid the Collapse of the Van Sweringen Empire Wherein Morgan and the Guaranty Trust Company Were Personally Interested and Not to Save the Investment of the Noteholders.

Throughout the affidavits there is the assertion that the motive of Morgan and of the Trustee was to avoid bankruptcy of the Van Sweringen Corporation and to apply all of the "segregated assets" and "assigned securities" for the exclusive benefit of the noteholders. We have shown above that no bankruptcy was possible and that this was not the motive. The real purpose was to avoid the bankruptcy of the "borrowers" whereby Morgan and Guaranty Trust Company stood to lose their $22,000,000 (R. 42). The Guaranty Trust Company and Morgan participated in the scheme to prevent the bankruptcy of "Vaness," whose $16,000,000 note it held and the bankruptcy of the Subsidiary which owed them $23,500,000, and which companies were unable to meet the interest payment which was due November 1, 1931. The real purpose was to prevent an acceleration of the note issue whereby the noteholders would have received all of the "assigned securities" and "segregated assets" in satisfaction of one-half of the note issue, and they would have received a deficiency decree for the balance, whereby they were able to enforce the open account in excess of $27,000,000 against the subsidiary, which owed Morgan and Guaranty Trust Company $23,500,000. **This is what they sought to avoid and what they did avoid.**

(e) It Was the Duty of the Trustee to Protect the Interest of the Noteholders Which It Failed to Do Because of Its Adverse Interest.

The Guaranty Trust Company, The Trustee under the note issue, entered into an agreement with Van Sweringens "for the exclusive protection of the $30,000,000 note issue" (R. 105). The agreement provided that the securities be held by the corporation in "**trust**" for the noteholders. Under the terms of the agreement the Trustee had the "exclusive" right of action to enforce the agreement. The Trustee, according to the affidavits, was a party to the secret agreement between Morgan and the Van Sweringens to prevent the acceleration and misapplication of the "segregated assets". It had knowledge that the corporation had no funds to meet its interest payment on November 1, 1931 and that a secret agreement was made to circumvent the application of the "segregated assets". It actively participated in such a scheme. It cannot escape liability. As Trustee of the note issue it had the power to accelerate the note issue and to resort to the "segregated assets" and "assigned securities" and to obtain a deficiency decree against the remainder of the assets. It participated in a deal whereby the "segregated assets" and "assigned securities" were used for the personal benefit of the Van Sweringens, Morgan, and itself. The noteholders were eliminated as creditors and Morgan and the Trustee were enabled to acquire over $13,784,000 in notes **to become the sole creditors of the Van Sweringen Corporation** and to receive the excess money from the "assigned securities" in application of a debt due from "Vaness". This was a breach of trust duties and obligations and they are liable for such breach. *New York Trust Company* v. *Michigan Traction Co.*, 193 F. 175.

Because of the adverse position of the Trustee it was its duty to either **resign,** or to **disclose** all the information to the noteholders. Whether or not bankruptcy or insolvency would have produced more or less than 50c on the dollar is of no importance. **The noteholders had the right to know the real truth and to determine for themselves what was best, when the Trustee** (who was selected to protect their interest) was not able to give the protection because of its **adverse** position. The fact that the Trustee lent its aid by loaning $11,000,000 in 1930 to make good the "segregated assets" in order to avoid the collapse of the entire Van Sweringen Empire is of no importance. **The fact is that in 1931 there were sufficient assets in the "segregated assets" to pay 50% to the noteholders.** The Trustee derived the benefit in that it avoided insolvency proceedings against the **top** holding company, Vaness, the **holding** company, Van Sweringen, and its **subsidiary,** Terminal, in selling the collateral prior to **such insolvency proceedings,** in obtaining its allowance of a claim in excess of $27,000,000 and **eliminating the noteholders as creditors.** The Trustee **personally benefited from the exchange** in that it received over $13,000,000 in notes in exchange of the **worthless stock** which it held as collateral. It, therefore, violated its trust duties to gain personal benefit and it is liable for such breach of trust.

V.

Federal Courts May Take Judicial Notice of Official Reports of Congressional Committees, and the Official Report of the Congressional Committee Conclusively Demonstrates the Fraud, the Violation of the Trusts, and the Damage Sustained.

Subsequent to the rendition of the opinion by the District Court plaintiffs' counsel received the official printed copy of Report No. 714, Part 3, on S. Resolution 71 of the 74th Congress dealing with the particular subject matter. The District Court was asked to reconsider its opinion in the light of the Report or to allow the case to be reopened.

The court failed to consider it when it entered its final judgment. A motion was made in the Circuit Court of Appeals for leave to file the Record. The Circuit Court of Appeals denied the motion on the ground that this Report was not made a part of the Record (R. 153). We cannot see how we could have made it a part of the Record when the Report was submitted to the court after it had rendered the opinion, and when it thereafter entered the judgment there was no opportunity to make this Report a part of the Record. We asked leave of the Circuit Court of Appeals to consider the Report but it refused. It is our position that the official report of the Senate Committee may be judicially noticed without making it a part of the Record. This Court considered the official report of a Senate Committee in *Arizona* v. *California*, 283 U. S. 423. It also received similar reports in *Tempel* v. *United States*, 248 U. S. 121, and this Court may now consider this Report.

In Chapter XV, pp. 871-906 of the Report, the floating of the $30,000,000 note issue is described in detail, with the active participation of the Guaranty Trust Company, and there is attached thereto the underwriting agreement wherein the Guaranty Company of New York, its wholly owned subsidiary, undertook to sell the notes at a consideration of $3,500,000 in commission (See page 1020 of the Report). In order to evade the various Blue Sky Laws of the states they resorted to placing the bonds on the Exchange. In addition to the $3,500,000 in commissions, J. P. Morgan & Co. was to receive 20,000 in warrants for its share (See page 1038). Chapter XXIV deals with the 1930 crisis leading up to the loan of the Guaranty Trust and Morgan in the amount of $22,000,000 (pp. 907-930). The rescue loan is described in Chapter XXVIII, pp. 931-958, and the "1931 crisis" which lead to the "offer" whereby the noteholders were defrauded to the extent of over $15,000,000 is vividly described in Chapter XXVIII, pp. 959-987. A reading of this Report will convince this Court of the justice of our cause.

For the reasons above stated we respectfully submit that the writ of *certiorari* be issued.

Respectfully submitted,

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FILED
DEC 1 1942
CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1942

No. 516

EUNICE E. EASTMAN,

Petitioner,

vs.

GUARANTY TRUST COMPANY OF NEW YORK, and GEORGE WHITNEY, as a member of the firm of J. P. Morgan & Co.,

Respondents.

BRIEF ON BEHALF OF RESPONDENTS IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

RALPH M. CARSON,
Counsel for Respondents.

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OPINIONS BELOW

The opinion of the District Court (R. 129-44) appears in 43 F. Supp. 637. The opinion of the Circuit Court of Appeals for the Second Circuit (R. 152-7) is reported in 130 F. (2d) 300.

JURISDICTION

Petitioner invokes the jurisdiction of this Court under Judicial Code § 240-A, as amended by the Act of February 13, 1925.

STATEMENT

The petitioner is the sole remaining plaintiff, the complaint having been previously dismissed as against all the other plaintiffs on jurisdictional grounds. 117 F. (2d) 95, cert. den. 313 U. S. 559.

The complaint as amended charged that plaintiff Eastman was wrongfully induced by defendants to exchange $10,000 principal amount of 6% notes issued by Van Sweringen Corporation under an offer made on October 29, 1931 (R. 3-9).

After service of their answer respondents answered extensive requests for admissions and written interrogatories propounded by plaintiff (R. 127) and took her deposition upon oral examination (R. 51). They then moved for summary judgment (R. 14). Plaintiff made a cross-motion for summary judgment relying solely upon respondents' moving papers and the record in the case (R. 50) thus conceding that no issue of fact was involved. The District Court granted respondents' motion and judgment was entered dismissing the complaint on the merits (R. 144-5). The Court of Appeals unanimously affirmed.

The claims asserted by the plaintiff and the facts surrounding the making of the exchange offer are summarized in the opinions below (R. 129-44, 152-7), and need not be restated.

The frequently misleading use which petitioner makes of the record is best dealt with by reviewing her contentions on the merits, which review will show the absence of any question justifying certiorari.

QUESTIONS PRESENTED

The questions of law presented on the undisputed evidence in the record relative to the exchange offer of October 29, 1931 are:

1. Whether the defendants committed fraud on the plaintiff Eastman.

2. Whether there was a breach of trust subjecting the defendants to liability.

ARGUMENT

POINT I

THE ESSENTIAL ELEMENTS OF AN ACTION FOR MISREPRESENTATION ARE COMPLETELY LACKING.

The five essential requirements of a fraud action are representation, falsity, scienter, deception and injury. *Ochs* v. *Woods*, 221 N. Y. 335, 338. Plaintiff herself disclaimed the first of these on her deposition and failed to raise any issue of fact as to the other four.

1. No Misrepresentation by Defendants.

The printed form of exchange offer dated October 29, 1931, and signed by Van Sweringen Corporation was sent to plaintiff by her brokers, Lee Higginson & Co., from whom she originally purchased the notes at 77½ in February 1931, and who recommended acceptance of the offer (R. 52-3, 70-3). Plaintiff admitted that no letters were received from Guaranty Trust Company, J. P. Morgan & Co. or Guaranty Company in connection with the offer, and that she did not discuss it orally with anyone connected with those companies (R. 56). This fact is corroborated by defendants' own affidavits (R. 15, 47).

2. Falsity, Scienter, Deception and Injury Not Proved.

There was likewise no falsity. No claim was made in the amended complaint or by plaintiff in her deposition that the offer itself contained any misrepresentations. Although it was claimed in the complaint (R. 7-8) that the noteholders including plaintiff were deceived by the balance sheet of Van Sweringen Corporation and its subsidiary

Cleveland Terminals Building Corporation, dated September 30, 1931, plaintiff adduced no proof that any of the figures or data contained therein were false or incorrect. It is undisputed that this balance sheet was received by plaintiff either from Van Sweringen Corporation or from Lee Higginson & Co. and not from defendants (R. 53).

Even if we assume that the offer was in reality that of defendants, as plaintiff's counsel suggests (br. pp. 36-7), and that defendants were responsible for the drafting of the balance sheet, they still would not be liable for fraud. Plaintiff did not pretend to have been deceived by any of the statements appearing in the offer itself. There was no proof of any deception as to the value of the common stock of Van Sweringen Corporation received by plaintiff under the offer. There were no statements as to the stock except such as appeared in the balance sheet (R. 62-9), and plaintiff was clearly not deceived by the form of the balance sheet. She testified on her deposition that she and her father, who was the owner of a printing business, had looked over the balance sheet (R. 52-3, 55, 59). Anyone examining the same would necessarily have realized that the stock of Van Sweringen Corporation at that particular time had little, if any, market value.[1]

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[1]Statements made by plaintiff's counsel to the effect that the defendants in their moving papers admit that an analysis of the balance sheet showed that the stock was worthless in October 1931 (br., p. 32) and that they knew it was worthless at that time, are not true. Although from their examination of the balance sheet they realized that its market value at the time of the offer was little or nothing, it could not be said that the stock was worthless because if there were a general economic recovery, which everyone was anticipating at that time, or an improvement in the Cleveland real estate situation, the stock would in all probability have reflected such recovery and increased in value accord-

The balance sheet showed that the only assets of Van Sweringen Corporation besides cash on deposit of less than $2,000 and the remaining segregated assets and assigned securities valued at about $13,444,000, were an investment in the entire capital stock of Cleveland Terminals Building Company and an open account for advances made to that company of over $27,000,000. Although the balance sheet listed the stock of Cleveland Terminals Building Company at approximately $29,250,000, it was there stated that this represented its cost at date of acquisition "without giving effect to adjustment in market value of listed securities owned" by Cleveland Terminals Building Company. Reference was then made to the attached balance sheet of Cleveland Terminals Building Company which set forth that the listed stocks which it owned, all of which were stated as having been pledged as collateral, had shrunk in value from approximately $38,000,000 in September 1930 to approximately $8,260,000 in September 1931. The cost of these securities was listed at about $37,232,000 in the Cleveland Terminals Building Company balance sheet. As the District Court pointed out in its opinion (R. 134), the difference between cost and market, *i.e.* about $29,000,000, practically wiped out Van Sweringen Corporation's investment

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ingly. In the light of subsequent events, the stock did prove worthless, but it was impossible to estimate in October 1931 what its true value might be in the event of such a recovery. As the District Court said (R. 142):

> "What the stock was then worth was problematical. Both sides now admit that it was worthless, but who could then tell? In judging their acts, we must look at the facts as they existed at the time, not aided or enlightened by those which subsequently took place. *Purdy* v. *Lynch*, 145 N. Y. 462. A wisdom developed after an event is a standard no man should be adjudged by. *Costello* v. *Costello*, 209 N. Y. 252-262."

in the stock of its subsidiary, shown as one of the principal assets on the balance sheet.

The balance sheet further showed that Van Sweringen Corporation had a total deficit on September 30, 1931, of over $2,120,000 and a loss for the first nine months of 1931 of nearly $1,300,000. In fact plaintiff testified that she must have seen this deficit when she looked over the balance sheet (R. 55). It also showed that Cleveland Terminals Building Company had sustained a net loss of over $1,600,000 for that same period.

The doubtful value of the open account of Cleveland Terminals Building Company was further demonstrated by its balance sheet which showed that nearly all of its assets, outside of securities, consisted of investments in Cleveland real estate, which plaintiff assumed was depressed at that time (R. 57). Moreover, among the liabilities of Cleveland Terminals Building Company listed on the balance sheet was nearly $24,000,000 principal amount of various mortgage bonds issued by it, $4,000,000 of which Van Sweringen Corporation had contingently guaranteed.

As a matter of fact, plaintiff did not rely upon the balance sheet at all in determining whether or not to accept the offer of Van Sweringen Corporation. In reaching that decision she really relied upon the judgment and advice of her father, who was a man of some business standing in the community (R. 56), and who, from his study of the balance sheet, would have seen that the stock offered to the noteholders in addition to the cash had little if any value at that time.

Plaintiff also failed to prove that she suffered any injury as the result of the offer. She received 50 cents on the dollar for the notes which had been selling in the market

for approximately 30 shortly prior to the offer (R. 25, 43). She also received 3 cents on the dollar as interest. Her own counsel admits (br. pp. 27-8) that the segregated assets and assigned securities were insufficient to the extent of $453,000 to pay 50 cents on the dollar to each noteholder and interest. No effort was made by plaintiff to prove how she would have fared if the offer had not been made, or that she would have realized more than 53 cents on the dollar if default had occurred in November 1931 and legal proceedings had been instituted to collect the open account owed by Cleveland Terminals Building Company to Van Sweringen Corporation. Speculation cannot be substituted for actual proof of injury.

Not one of the five elements necessary for recovery in an action for misrepresentation exists here. Plaintiff did not even attempt to raise an issue of fact in this respect.

POINT II

THERE WAS NO BREACH OF TRUST.

The District Court followed the admonition of Rule 8(f) of the Rules of Civil Procedure that a pleading should be "construed as to do substantial justice", and afforded plaintiff every possible benefit on the motions for summary judgment by construing the complaint as "alleging rather inartistically not only misrepresentation but possibly a breach of trust" (R. 132).

1. There Was No Trust or Fiduciary Relationship Between Defendants and Plaintiff.

Obviously, no fiduciary or trust relationship existed between plaintiff and J. P. Morgan & Co. It did not partici-

pate in the original issue of the notes. It had no dealings with plaintiff or the other noteholders.

There was likewise no trust or fiduciary relationship between Guaranty Trust Company and the plaintiff or any of the other noteholders. Although Guaranty Trust Company was named as "trustee" in the so-called trust indenture (R. 75-105) under which the notes were issued, there was no real trust because there was no trust *res*. In order to have a valid trust there must be a trust *res*.

> *Bradford* v. *Chase National Bank,* 24 F. Supp. 28, aff'd 105 F. (2d) 1101, aff'd 309 U. S. 632;
> Scott—*The Law of Trusts,* § 2.6.

See to the same effect:

> *Bank of America* v. *Scully,* 92 F. (2d) 97 (C. C. A. 10);
> *Collins* v. *Mosher,* 91 F. (2d) 582 (C. C. A. 9);
> *American Surety Company* v. *Baldwin,* 90 F. (2d) 708 (C. C. A. 7);
> *In re United Cigar Stores Co.,* 70 F. (2d) 313, 315 (C. C. A. 2);
> *Hickok* v. *Bunting,* 67 A. D. (N. Y.) 560, 562;
> *City Bank Farmers Trust Co.* v. *Charity Organization Society,* 238 A. D. 720; aff'd 264 N. Y. 441.

The trust indenture dated May 1, 1930 between Van Sweringen Corporation and Guaranty Trust Company (R. 75-105) made no provision for the holding of any property by Guaranty Trust Company for the benefit of the note-

holders. It is clear from a reading of the indenture that there was no trust *res*.

The notes themselves specifically refer the noteholders to the indenture "for a description of the terms on which such notes are issued and of the rights of the Trustee and of the holders of the notes under said Indenture" (R. 76-7). Neither the notes nor the indenture state that the notes are secured by anything.

The indenture provided that contemporaneously with the issue of the notes the Van Sweringen Corporation would acquire, free from any lien or encumbrance, 500,000 shares of Alleghany Corporation, to be known as "segregated assets" (R. 83-4). The indenture further provided (R. 85) that whenever the aggregate value of the segregated assets should exceed 50% of the aggregate principal amount of the notes then outstanding, the corporation could use such excess for its general corporate purposes. The parties were explicit in providing that the segregated assets should not constitute collateral security or a pledge for the payment of the notes (R. 84).

Likewise, the so-called "assigned securities" were not to be held in trust. The agreement of May 1, 1930 (R. 105-11) relating to these securities, provided that whenever the value of the segregated assets should be less than 50% of the principal amount of the outstanding notes, the Messrs. Van Sweringen would repair such deficiency by assigning and delivering to Van Sweringen Corporation readily marketable securities in the amount of such deficiency (R. 106-7). In consideration of the assignment and delivery of the marketable securities under this agreement Van Sweringen Corporation was required to deliver to the

Messrs. Van Sweringen stock or obligations of the corporation (R. 107).

The assigned securities belonged to Van Sweringen Corporation after their assignment and delivery from the Messrs. Van Sweringen. These securities were "available to the creditors of the Corporation for application to the payment of its debts and liabilities" (R. 86, 107-8). Moreover, the corporation could dispose of them to provide funds necessary for the payment of indebtedness when it did not have cash available for that purpose (R. 88, 109). They were not to be held in trust for the noteholders by the corporation. Only the notes or obligations given to the Messrs. Van Sweringen by the corporation in consideration of the assignment and delivery of these securities were to be held in trust for the noteholders and then only in the event of liquidation and a deficiency in the payment of the $30,000,000 note issue (R. 86, 107). This is the so-called "property in trust" referred to in plaintiff's brief (p. 18).

The agreement of May 1, 1930 (R. 105-11) relating to the assigned securities clearly did not constitute a trust *res* as plaintiff's counsel suggests (br. p. 23). It was not held by Guaranty Trust Company for the benefit of the noteholders. Guaranty Trust Company was not under any duty to institute any proceedings for the enforcement of its provisions unless requested to do so in writing and upon being indemnified to its satisfaction. It was "under no duty" to the noteholders in the absence of such request and indemnity (R. 110-11).

Guaranty Trust Company did not have title to or possession of the segregated assets or assigned securities. It never held them for the benefit of the noteholders. At all

times they were owned by and kept in the possession of Van Sweringen Corporation (R. 30). In fact no property of any kind was ever held by Guaranty Trust Company in trust or for the benefit of the noteholders.

The rights and powers given to Guaranty Trust Company under the so-called trust indenture and the duties imposed upon it by the indenture did not create any fiduciary relationship in the absence of a trust *res*. The duties were routine in nature and for the most part discretionary. For example, Guaranty Trust Company had to authenticate the notes issued under the indenture (R. 80), receive and pay the interest and principal of the notes at its principal office in New York City (R. 76), and receive information, financial statements and balance sheets of the corporation with respect to which it had no duty or obligation whatsoever (R. 89-90). It could declare the principal due in the event of any default and had certain other discretionary powers. But it was not bound to institute legal proceedings unless the holders of at least 25% of the principal amount of the outstanding notes requested it to do so, and furnished it with satisfactory indemnity (R. 92-3, 98). If Guaranty Trust Company then refused to proceed within a reasonable time the noteholders were empowered to institute proceedings (R. 96-7), so that plaintiff's statement (br. pp. 21-2) that Section 24 of the indenture vested Guaranty Trust Company with the exclusive right of action is inaccurate.

The courts below did not overlook the fundamental law of trusts as charged by plaintiff's counsel (br. pp. 20-3). They properly followed the authorities previously cited in holding that there could be no trust relationship in the absence of a *res*.

In *Farmers Loan & Trust Co.* v. *Lake Street R. R. Co.*, 173 Ill. 439, 51 N. E. 55, relied upon by plaintiff (br. p. 22), there was an actual trust *res*, the obligor of the bonds involved having given a mortgage and trust deed to the trustee. This is likewise true in *Straus* v. *Chicago Title & Trust Co.*, 273 Ill. App. 63, also cited by plaintiff (br. p. 23). Moreover, plaintiff's summary (br. p. 21) of Professor Scott's statement in § 2.2 of his *The Law of Trusts* is quite inaccurate.

Since no fiduciary relationship existed as between Guaranty Trust Company and the plaintiff or any of the other noteholders, there could be no breach of trust by defendants.

2. The Defendants Neither Received Any Part of the Segregated Assets or Assigned Securities Nor Benefited by the Offer.

The disposition of the segregated assets and assigned securities is set forth in detail in Mr. Whitney's affidavit (R. 30-3). It is there definitely shown that the defendants received no part of these securities or the proceeds thereof. These facts were not contradicted by plaintiff on the motion for summary judgment and stand undisputed. The affidavits also completely disprove the charge made by plaintiff's counsel in the complaint that defendants appropriated all other available assets of Van Sweringen Corporation and its subsidiary Cleveland Terminals Building Company (R. 29-33).

Plaintiff's counsel states again and again in his brief that by means of the offer defendants were able to substitute $13,784,000 of the notes in place of worthless stock of Van Sweringen Corporation as collateral for the bank

loans. This is a most misleading statement. When $15,000,000 principal amount of the notes was retired under the offer the defendants and the other banks participating in the loan to Vaness Company could have insisted that the remaining assigned securities totaling approximately $7,514,000 be pledged for the loan (R. 27). This right was recognized in the agreement of October 29, 1931 (R. 122-3). The bankers (including not only the defendants but seven other banks and bankers, R. 19) in consenting to the making of the offer relinquished their right to this collateral and in return Vaness Company agreed to give the notes acquired by it under the offer to the bankers as collateral for its loan (R. 123).

Although the bankers also agreed to and did release stock of Van Sweringen Corporation needed for the offer, the notes were not received by them in place of said stock but in place of the assigned securities, as the agreement of October 29, 1931 clearly shows (R. 123).

The bankers thus released their right to over $7,500,000 of the assigned securities, consisting of United States Government obligations and cash, so that the offer could be made to all noteholders, assuring them 50 cents on the dollar plus interest, in return for $13,784,000 of the Van Sweringen notes which shortly before the making of the offer had been selling on the market for about 30 cents on the dollar.

Moreover, the bankers did not use these notes as a means of collecting the open account of approximately $27,000,000 owed by Cleveland Terminals Building Company to Van Sweringen Corporation and took no advantage of their position in this regard even after Van Sweringen Corporation defaulted in the payment of interest

after November 1932. They merely held the notes as part of the collateral securing the loans until September 1935 when the collateral was sold at public auction (R. 35). Prior to the auction, after a careful study by the banking group, it was decided that the value of the notes was so problematical and in any case so small that no protective bid would be put in for the notes at the auction, and the banking group did not bid for them (R. 46). The collateral underlying not only the Vaness loan but the Cleveland Terminals Building Company loan was sold at the auction for $4,703,000 and the bankers realized only about 12 cents on the dollar (R. 35).

Since the defendants received no part of the segregated assets and assigned securities and did not benefit by the offer in any way, the cases cited by plaintiff's counsel at pages 37-40 of his brief, relating to fraud and breach of trust, have no application, even if we assume some fraud or breach of trust was practiced on plaintiff.

3. Assuming the Existence of a Fiduciary Relationship Between Guaranty Trust Company and the Noteholders, There Was No Violation of Duty.

The circumstances which induced the making of the offer to noteholders are set forth in detail in the affidavits (R. 15-49). The moving consideration for making the offer, in so far as defendants were concerned, was to stop the private purchase of notes by Van Sweringen Corporation with the segregated assets, even though such purchase was permissible under the terms of the indenture (R. 24, 38, 84-5). If these purchases continued, the result would be to reduce the outstanding notes to $15,000,000 and release the segregated assets and assigned securities from the

terms of the indenture (R. 24-5, 38-9). The Van Sweringens would then have free disposal of these assets subject, of course, to the rights of the New York banking group to require the deposit of the assigned securities as additional collateral for the bank loans (R. 27, 43, 49). This would leave the remaining half of the note issue without the protection of these securities.

The situation became even more alarming when, as the market value of the notes declined, Van Sweringen Corporation after the middle of September 1931 was able to buy notes at less than 50 cents on the dollar. In October the notes went down as low as the 30's (R. 43, 48). The result of these purchases at less than 50 was to make the securities available to the Van Sweringen interests in amounts greater than the purchase price (R. 25). In fact, nearly $4,000,000 of notes had been purchased at an average price of less than 50 cents on the dollar by the Van Sweringens before the making of the offer (R. 30).

It was realized that the banking group could throw Vaness Company and Cleveland Terminals Building Company into bankruptcy by calling the bank loans unless interest were paid on November 1, 1931, which because of the financial condition of the borrowers seemed unlikely (R. 39). If the banks were able in this way to force the subsidiary and also the parent of Van Sweringen Corporation into bankruptcy, Van Sweringen Corporation itself would probably have gone into bankruptcy, either voluntarily or involuntarily by action taken by Guaranty Trust Company on behalf of the creditor noteholders. Its only asset outside of the segregated assets and assigned securities, stockholdings in Cleveland Terminals Building Company and the open account indebtedness owed by the latter,

was less than $2,000 in cash (R. 64). Even if, as plaintiff claims, its only creditors were the noteholders, and even if we disregard its conditional liability as guarantor of an $8,000,000 note issue of Cleveland Terminals Building Company until one-half thereof had been paid (R. 64), which in all probability would have matured in the event of the latter's bankruptcy, the segregated assets and assigned securities would have been diluted to a great extent by the fees and expenses incident to a bankruptcy proceeding (R. 41-2). In this connection it should be recalled that at the time of the offer the segregated assets and assigned securities admittedly (pltf.'s br., pp. 27-8) were insufficient to pay every outstanding noteholder 50 cents on the dollar plus the November 1 interest. Moreover, there was the possibility which was considered by the defendants that a bankruptcy trustee might utilize a portion of these securities in an attempt to salvage the real estate holdings of Cleveland Terminals Building Company for the possible benefit of Van Sweringen Corporation creditors (R. 42).

We have already demonstrated the doubtful value of the $27,000,000 open account of Cleveland Terminals Building Company (pp. 5-6). Most of its assets consisted of mortgaged real estate holdings (R. 40, 66-7). Because of the condition of Cleveland real estate it would have been futile to try to realize on the equities of these holdings at that time (R. 26). All of its securities were pledged (R. 66). Among the liabilities listed on its balance sheet of September 30, 1931 were nearly $24,000,000 principal amount of various mortgage bonds issued by it (R. 67). Its balance sheet showed a net loss of over $1,600,000 for the first nine months of 1931 (R. 69). Moreover, the New York banks which made the large loan to Cleveland Termi-

nals Building Company in October 1930 (even if we eliminate entirely Guaranty Trust Company's participation therein), would have had a claim for any deficiency resulting after a forced sale of the collateral. Such a claim would have been on a parity with that of Van Sweringen Corporation for the $27,000,000 open account in any bankruptcy proceeding involving Cleveland Terminals Building Company (R. 42).

After the fullest consideration the defendants could only come to the conclusion that the alternative of possible insolvency proceedings offered no real prospect of the noteholders getting 50 cents on the dollar (R. 26, 43, 49). Furthermore, they could not hope for any immediate recovery in a bankruptcy proceeding. The best solution, from the standpoint of the noteholders, for the problem brought about by the decline in market values and particularly by the private purchase of the notes by the Van Sweringen interests, was to persuade Van Sweringen Corporation to pay the noteholders 50 cents on the dollar plus interest to November 1. Every noteholder would thereby be definitely assured of sharing equally and immediately in the segregated assets and assigned securities.

The common stock of Van Sweringen Corporation was also included in the offer at the suggestion of the Van Sweringens. Defendants believed this only fair to the noteholders so that they might have some interest in the equity of the corporation, whatever it might be, in the event security values and particularly Cleveland real estate should improve from the effects of the depression (R. 26-7, 44).

If defendants had really wished to harm the noteholders for their own personal gain, they could have done so merely

by lending the Van Sweringen Corporation the necessary funds to make the November 1 interest payment, if such funds could not have been obtained by other means, and by permitting and even encouraging Van Sweringen Corporation to continue the purchase of notes with the segregated assets. When $15,000,000 of the notes had been retired, defendants could then have insisted that the balance of the assigned securities be delivered to them as additional collateral (R. 27, 48-9). But, as has been said, they waived their rights in this respect so that all noteholders would be treated equally and could share alike in these securities.

By reason of the offer the noteholders were able to get 53 cents on the dollar in November 1931 for their notes which had been selling in the 30's just before the making of the offer, while the bankers, who are accused of having served their own interests in sponsoring the offer, realized only about 12 cents on the dollar on their loans after the collateral was sold in September 1935.

4. Plaintiff Suffered No Loss by Reason of the Exchange.

The Circuit Court was correct in holding that even assuming a fiduciary relationship, there was no proof of injury to plaintiff by reason of defendants' acts. As previously pointed out, the segregated assets and assigned securities in themselves were not sufficient to pay each noteholder 50 cents on the dollar plus the November 1, 1931 interest. The only other available asset of Van Sweringen Corporation was the open account indebtedness owed to it by its subsidiary Cleveland Terminals Building Company. This account was practically if not entirely worthless. Although the defendants' affidavits and the exhibits thereto annexed clearly demonstrated that in all probability plaintiff would not have realized 53 cents on the dollar

had the offer not been made, plaintiff offered no proof of any kind to the contrary, and even based her own motion for summary judgment on these same affidavits and exhibits. Plaintiff's counsel misrepresents the Circuit Court's opinion in stating that it concluded that the open account indebtedness of Cleveland Terminals Building Company was "of doubtful value" (br. pp. 25-6). The court after using the words "doubtful open account" immediately said (130 F. [2d] at 303):

> "A glance at the balance sheet of that company shows that even this debt was practically, if not entirely, worthless. . . ."

The decision of the Circuit Court of Appeals is not in conflict with the decisions in *McElwain* v. *Wickwire Spencer Steel Co.*, 126 F. (2d) 210, and *Miller* v. *Miller*, 122 F. (2d) 209, as contended in plaintiff's brief (pp. 10, 25). In both of these cases the proof adduced by the respective parties showed a substantial dispute of fact. In the present case, as we have already shown, no issue of fact exists. There must be a genuine issue as to a material fact in order to justify a denial of a defendant's motion for summary judgment. *Banco de Espana* v. *Federal Reserve Bank*, 28 F. Supp. 958, 973, aff'd in 114 F. (2d) 438.

POINT III

THE CIRCUIT COURT OF APPEALS PROPERLY DENIED PLAINTIFF'S MOTION TO HAVE THE RECORD AMENDED SO AS TO INCLUDE SENATE REPORT NO. 714, PART 3.

The report is a highly partisan and biased treatment of hearsay material and does not meet the requirements of Rule 56(e) relating to motions for summary judgment.

Moreover plaintiff's counsel made no application to have the District Court consider the material contained therein, as shown in the affidavit of defendants in the Circuit Court, which plaintiff has not included in the record now before this Court. Plaintiff did not request that she be given an opportunity to furnish any of the material set forth in the report in the form required by Rule 56(e). She did not apply for reargument on the basis of the report. No application was ever made to enlarge the record so as to include this report before the record was filed in the Circuit Court. In fact, plaintiff's application to that court to consider the report on her appeal was not made until defendants, as respondents, had already served and filed their brief.

The reports which this Court considered in *Arizona* v. *California,* 283 U. S. 423, involving the Boulder Dam project, and *Tempel* v. *United States,* 248 U. S. 121, involving the improvement of the Chicago River, present no parallel to the present situation. Clearly the ruling of lower courts on the admission of evidence is not a ground of certiorari.

CONCLUSION

This case does not present questions of any particular gravity or general importance. The legal questions raised are quite elementary. The decision of the Circuit Court of Appeals, which petitioner desires to have reviewed, is in full accord with the decisions of this Court, and does not conflict with decisions made by Circuit Courts of Appeals in the other circuits. Moreover, there has been no misin-

terpretation of the Federal statutes or the Rules of Civil Procedure.

For the foregoing reasons the petition for a writ of certiorari should be denied.

Respectfully submitted,

RALPH M. CARSON,
Counsel for Respondents.

November 28, 1942.

(3)

DEC 10 1942

CHARLES ELMORE CROPLEY
CLERK

Supreme Court of the United States

OCTOBER TERM, A. D. 1942.

No. 516

EUNICE E. EASTMAN,
Petitioner,

vs.

GUARANTY TRUST COMPANY OF NEW YORK, ET AL.,
Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

REPLY BRIEF.

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PETITIONER'S REPLY.

Respondents say (p. 7) that there was no breach of trust because: (1) there was no trust or fiduciary relationship between the respondents and the petitioner and (2) that the respondents did not receive any part of the

segregated assets and did not benefit by the offer. They also say that even assuming the existence of a fiduciary relationship there was no violation of duty, and petitioner suffered no loss by reason of the exchange. We will reply to the points and show that they are without merit.

The Trust Relationship. The proposition that there was no trust relationship is founded upon the contention that there was no trust *res*. The authorities cited in the petition (pp. 20-21) on the point that the transfer of the *rights* of the beneficiaries to the Trustee was in itself sufficient to constitute a trust *res*, are nowhere discussed in respondents' answer. The authorities which they cite may be applicable upon an issue between attaching judgment creditors and the Trustee prior to entry in possession or taking other steps to foreclose. In such a case the fact that the Trustee was not possessed of the trust assets might be of importance as to which lien attached first. The *Baldwin* case (90 F. (2d) 708) which they cited is one of such cases. This has *no bearing upon the question of the fiduciary or* trust relationship between the parties (*Flannery* v. *Flannery Bolt Co.*, 108 F. (2d) 531, 534).

The *Bradford* case (24 F. Supp. 28) which is cited by the court and by respondents dealt with a *constructive trust* and there being no trust *res* there could be no constructive trust. There, it was pointed out that a trust *res* may consist of a "chose in action" and the conclusion that there was no trust *res* was because there it was sought "to make a *res* out of a liability or to impress a trust therein". Here, it is sought to hold the Trustee liable for a breach of a trust duty relating to trust property which the trustee appropriated to its own use.

The *United States Cigar Store* case (70 F. (2d) 313) on which respondents rely is based on the fact that "there was no segregation" of the funds and there was no "putting aside" of such funds. Here, there were "segregated assets" and there was "put aside" the "assigned securities". The fact that the "assigned securities" were put away with the corporation is not of importance according to that decision. *This is especially true when the property which was put aside did not belong to the corporation but belonged to others who placed the securities with the corporation for a specific purpose.* Thereby a trust was created under the decision of this court (159 U. S. 312) cited there.

The *Bank of America* case (92 F. (2d) 97) which is relied on, involved a question between beneficiaries of a trust and creditors on the point whether the beneficiaries were partners. It was not a question whether the trust was valid *between the parties,* namely, the trustee and the beneficiaries.

The *Collins* case (91 F. (2d) 582) did not involve the question as to a trust *res* and only involved the question of an "equitable duty."

There is not a single authority which tends to support the proposition that as between the parties, the trustee and the beneficiaries, the former may be absolved from liability for a breach of trust on the ground that it was not possessed of a trust res, when it had the power to obtain the trust res in the event of a default, and all rights of action were vested in it.

The Trustee which *accepted its trust duties* and caused the notes to be issued *is in no position to claim that there was no trust and it is estopped from making such a de-*

fense. Having acquired all the rights and remedies from the noteholders it does not lie in its mouth to say that it had no trust relationship to them. While as against third parties possession may be necessary for the validity of a pledge it is not necessary between the parties. Title is not required for the validity of a pledge, nor is possession necessary for the validity of a trust (*Casey* v. *Cavarec,* 96 U. S. 467).

The "segregated assets" and "assigned securities" constituted pledged assets or a trust *res,* as long as no rights of third parties had intervened at the date of the "offer". The *"setting apart of designated personal property"* for the payment of a debt constituted a valid pledge between the parties (*Gluck* v. *Therme,* 154 Iowa 201; *Casey* v. *Cavarec,* 96 U. S. 467; *Sammet* v. *Mayer,* 108 F. (2d) 337, C. C. A. 2).

The part of the agreement which provided that the "segregated assets" shall not be "deemed" as a pledge or mortgage was repugnant to the previous provisions of the trust instrument containing elements of a pledge or mortgage and it is well settled that where two clauses are repugnant the first will be retained and the second rejected (*Thomas Hart Co.* v. *Newman Co.,* 365 Ill. 160, 166; 13 C. J., p. 536). Besides, *it did not apply to the "assigned securities" which were pledged.*

The Trust Res. The statement that the assigned securities were not to be held in trust is contrary to the record. The assigned securities were not the property of the corporation but belonged to its principal officers. Under the terms of the agreement these securities were to be deposited with the corporation and to be *held by it for specific purposes. The cor-*

poration was the agency of the Trustee, and all rights of action thereunder were vested in the Trustee. The agreement provided (R. 111):

> "The corporation agrees to receive, hold and dispose of such securities * * * under the provisions hereof."

It further provided:

> "This agreement is made for the exclusive benefit of the holders of said notes and the Van Sweringens."

This agreement, therefore, contradicts the statement of the respondents (p. 9) that the so-called assigned securities were not to be held in trust.

Benefits Received. The argument (p. 12) that the respondents did not receive any part of the segregated assets or assigned securities is refuted by the record. The offer stated that there was in the segregated assets and assigned securities, assets of $13,440,681.86 and there were outstanding securities of $26,234,000 (R. 71). It is shown by the record that $1,213,000 in notes were *not exchanged* (R. 34) and such notes did not participate in the segregated assets. Deducting the $1,213,000 from $26,234,000 there was left $25,021,000 which participated in the $13,440,681.80 to whom 50% was paid in cash, or $12,510,500. This left a balance of $930,181.80, which was turned over to the respondents under the secret agreement made with Morgan, which stated (R. 72) that "the remaining assigned securities will be withdrawn by the Van Sweringen interests" and it is shown by the affidavit of the respondents that all of these assigned securities were turned over to the respondents (R. 30-34). Besides, it is also shown (R. 33) that $65,779.21 was taken out from the

segregated assets to purchase a $71,000 participation in a $553,000 loan made in November, 1931 by J. P. Morgan & Co. to the Higbee Company.

The amount of the profit or gain is of no importance (*Anglo-Col. National Bank* v. *Lazard,* 106 F. (2d) 693).

In connection with petitioner's statement that as a result of the offer they were able to substitute $13,784,000 of the notes for the worthless stock as collateral, counsel say (p. 13) that: "This is a most misleading statement." *They do not deny that they received $13,784,000 in notes* and substituted them as collateral for the worthless common stock. They say that these notes were acquired in exchange for the "assigned securities" and not in exchange for the common stock. The fallacy of this contention is apparent. They were in no position to lay their hands on the "assigned securities" if the offer was not accepted. The only way they were able to obtain the assigned securities was by means of the offer whereby they cancelled the outstanding notes to the extent of $15,000,000 and thereby the assigned securities were released. *By one device or another they did substitute in their portfolio the $13,784,000 notes for the worthless stock as collateral.*

The statement that the bankers released their rights to over $7,500,000 of the assigned securities is unsupported by anything in the record.

The argument that the bankers did not use the notes to enforce collection of the $27,000,000 open account and merely held the notes as part of the collateral until September, 1935 when they were sold, is devoid of merit. The respondents were in control of the Van Swerinen

Empire and were not concerned with pressing their debts for collection. Their only concern was to prevent *other creditors from pressing their debts for collection and* thereby disrupt the empire. By the scheme employed the other creditors were eliminated and everything was placed in the control of the respondents who used the assets as long as they could milk them and when everything was gone they resorted to the sale followed by the bankruptcy.

Breach of Trust. The contention that if there was a fiduciary relationship there was no violation of duty, is also without merit. They say (p. 14) that the "moving consideration" for making the offer "was to stop the private purchase of the notes by the Van Sweringen Corporation with the segregated assets". Why were they, who claimed to have owed no fiduciary relationship to the noteholders, concerned in stopping such a purchase? If they did want to stop it all that was necessary for them to do was to inform the noteholders that there were available assets for them at 50c on the dollar and they certainly would not have sold the notes at 30c on the dollar. Whatever the motive might have been, it was the duty of the fiduciaries to inform the beneficiaries of the existing facts and not to conceal them from them. If it be true, as they now say (p. 17), that the respondents came to the conclusion that the only alternative was insolvency proceedings and that the offer of the common stock was only "in the event security values" improved, *this was not reflected in the offer which they then made public.*

Loss Sustained. The contention that the petitioner did not show any loss is contrary to the record. The matter was fully discussed in the petition for rehearing which was filed in the Circuit Court (R. 165-167) there is no need for repetition.

Elements of Fraud. The point (p. 3) that the essential elements of an action for misrepresentation are completely lacking, of course, involves the merits and is improper to be argued on a petition for writ of *certiorari*. Having raised the point, however, we will briefly answer it. The five elements are essential for "actual fraud" and *are not essential for a "constructive fraud"* embracing a breach of a fiduciary duty (26 C. J., pp. 1060-1; 23 Am. Jur., p. 757). If the petition will be granted we will then show that *all* of the necessary elements constituting an action for fraud were present.

The Senate Report. It is urged that the report of the Senate Commission should not be considered by this court. No authorities are cited. In another part of their brief counsel claim that J. P. Morgan & Co. were total *strangers*. Even the District Court held that by reason of the participation of J. P. Morgan with the Guaranty Trust Company in the $23,500,000 note *it stood in the same capacity as the Trustees* (R. 142). However, it appears from the Senate Report that J. P. Morgan participated in floating the $30,000,000 note issue and that its share of the compensation was 20,000 in warrants (See Senate Report 714, Part 3, Exhibit VS-590, page 1020, and Exhibit VS-598 at page 1038).

For the foregoing reasons we urge that the writ of *certiorari* be allowed.

Respectfully submitted,

MEYER ABRAMS,
BENNETT I. SCHLESSEL,
Counsel for Petitioner.

FILED
JAN 7 1943
CHARLES ELMORE CROPLEY
CLERK

Supreme Court of the United States

OCTOBER TERM, A. D. 1942.

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ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

PETITION FOR REHEARING.

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PETITION FOR REHEARING.

To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States:

Petitioner, Eunice E. Eastman, by her counsel hereby petitions for the allowance of a rehearing from the order denying the issuance of the writ of *certiorari* and as reason for application says:

Since the denial of the petition there were published two opinions bearing on the issue involved. The attention of petitioner's counsel was also called to an additional authority which is squarely in point.

Petitioner's counsel was also informed by the attorneys for the respondents that they intend to apply for a summary judgment in the second case which is now pending in the same District Court and which appears in the appendix of this record at page 168. They intend to urge that the decision in the instant case on the point that there was no trust relationship between the Guaranty Trust Company of New York and the note holders constitutes *res adjudicata* as to the second suit on behalf of the owners of $1,213,000 in notes who did not receive anything out of the segregated and assigned securities. Such a motion might prevail. While in the ordinary case the denial of *certiorari* does not constitute an affirmance, yet in the instant case, where the appeal would go to the same Circuit, the denial of the *certiorari* would in effect constitute an affirmance.

The Trust Relationship. On the question whether the trust indenture created a trust relationship, which was discussed in the petition (pp. 20-21) and in the Reply (pp. 2-4) petitioner's attention was called to a statement by Professor Scott in Vol. 1, Sec. 82, p. 450, which is as follows:

> "A legal claim or **a chose in action,** even if it is not represented by a specialty or other instrument as in case of bonds or shares of stock, can be held in trust. **Thus a creditor can create a trust of his claim against the debtor by transferring it to another as trustee.**"

The illustration of Professor Scott applies on all fours to the instant case, as the note holders, as creditors, transferred their rights of action to the Guaranty Trust Company in trust to enforce such rights and to enforce the covenants contained in the agreement with reference to the "segregated assets" and "assigned securities".

We stated in the petition that even if there were no trust *res* there was a *trust relationship* between the Guaranty Trust Company and the petitioner. This was held in *State* v. *Saratorin,* 130 S. W. 2nd 547 (Mo. 1939). There the court pointed out that "in the strict sense" a trustee is one who holds the legal title to property for the benefit of another, while in the "broad sense" the term is applied to *anyone standing in a fiduciary capacity,* and as authority for the statement it cited a decision of the court (110 U. S. 330).

Whether in the "strict sense" or in the "broad sense" *there was a trust relationship* established by the Guaranty Trust Company when it caused the $30,000,000 note issue to be floated on the market and when it *accepted the terms* of the trust "created" thereby (R. 104).

In connection with the petition for rehearing we ask the Court to examine the complaint (R. 168) filed on behalf of the owners of $1,230,000 in notes who did not receive anything out of the assigned securities and segregated assets by reason of the acts of the trustee and to *consider the effect of the decision and the denial of the certiorari* on the proposed motion of the respondents in the latter case to defeat the action by a defense of *res adjudicata.*

We also would like to refer this Court to the statement in Bogert on Trusts, Sec. 111, p. 349, as follows:

> "The property *interests* which the trustee holds are called the trust property, *trust res* or the subject matter of the trust."

It should be noted that it is not the "property," but the "interests" that *is the subject matter of the trust or res.* In the instant case the interests of the note holders in the property was *their right of action* and such interests were exclusively vested in the trustee. Therefore, there was a trust *res.*

The Two Decisions Published Subsequent to the Denial of the Petition.

Petitioner asked in her petition the following question (p. 20):

> "What was this Trust Indenture upon which the $30,000,000 in notes were floated on the market by the Trustee and by its Subsidiary whereby over $15,000,000 were lost to the investors?"

Even if the answer be that it was not a Trust, it was at least a contract establishing an agency, and thereby a fiduciary relationship was also established as held in a decision published December 23, 1942, subsequent to the denial of the petition (*Doner* v. *Phoenix Land Bank,* 381 Ill. 106). There, the Court said, p. 113:

> "The rule is that the relation of principal and agent is a fiduciary one. (*Quinn* v. *Phipps,* 113 So. (Fla.) 419, 54 A. L. R. 1173; *Dennis* v. *McCagg,* 32 Ill. 429.) The allegations in the complaint show an unequivocal act of agency by Westervelt. Whether he volunteers or agreed in response to appellant's efforts to save his property is immaterial. By assuming to act for appellant he took upon himself certain obligations, among which was the duty not to deal with the subject matter of the agency for his own advantage."

The Court also said:

> "The legal effect of the transaction for his own benefit was the creation of a constructive trust. The rule in this State is established by an unbroken line of decisions that anyone occupying a fiduciary rela-

> tion, such as an agent, trustee, partner, guardian, conservator, attorney, executor or administrator, cannot deal on his own account with any thing or the persons falling within that trust relationship. (*Dennis* v. *McCagg, supra; Suchy* v. *Hajicek,* 364 Ill. 502; *Pulfrey* v. *Wid,* 340 *id.* 553; *Pope* v. *Dapray,* 176 *id.* 478; *Kochorimbus* v. *Maggos,* 323 *id.* 510.) If anyone occupying such a relation deals with the subject matter of the relationship and thereby gains an advantage to himself he will be deemed guilty of fraud, either actual or constructive, depending upon his intent and purpose."

Whether or not there was a trust or an agency established there was in either case a confidential relationship which would entitle the petitioner to relief.

In the *Doner* case, *supra,* the Court also said at page 114:

> "Where it appears, as in this case, that the relation of trust and confidence existed by reason of the agency, the agent who has profited thereby has the burden of rebutting the presumption of fraud by clear and convincing proof that he has not betrayed the confidence reposed in him. (*Suchy* v. *Hajicek, supra; Pulfrey* v. *Wid, supra.*) Where one occupying such a relation to another, through any questionable means, gains something for himself, which in equity and good conscience he should not be permitted to keep, equity will raise a constructive trust and compel him to turn it over to the one equitably entitled to it, or to otherwise execute the trust as the court may direct."

The other case which was published subsequent to the filing of the petition is the decision in *Toebelsman* v. *Missouri-Kansas Pipe Line,* 130 F. (2d) 1016. In that case the Court construed Rule 56 and held that on a motion for a summary judgment the Court is in no position to pass

on any *factual* matter and on the question whether there was a factual matter to be decided the doubt must be resolved *against* the *movant*. This point is of importance on the question whether or not the trial court or the court of appeals had a right to decide the *factual* question whether the open account of $27,154,584 was of "doubtful" or "substantial" value.

This petition for rehearing presents the question whether one class of note holders who were defrauded of half of their debt by the trustee of the note issue may recover anything from the trustee for a breach of trust and whether another class of note holders who lost *their entire investment* as a result of breach of the trust by the trustee, which actively participated in the misapplication of the segregated assets and assigned securities may have no remedy because of the conclusion that the trust agreement did not constitute a trust. We hope that this Court will re-examine our petition and reply in the light of the new authorities cited above and particularly the effect of the denial of the application on the pending suit (R. 168) and that it will vacate the denial and allow the issuance of the writ.

Respectfully submitted,

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Counsel for Petitioner.

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Chicago, Illinois,
Of Counsel.

Certificate of Counsel.

The undersigned, Meyer Abrams, one of the attorneys for the petitioner, hereby certifies that he prepared the foregoing petition for rehearing, and that he is of the opinion that the petition is well founded in point of law, and is not interposed for the purpose of delay.

Chicago, January 5, 1943.

MEYER ABRAMS,
Counsel for Petitioner.